Financial statements

Financial Statements (continued)

Consolidated income statement / Consolidated statement of comprehensive income

Consolidated income statement for the year ended 31 December 2010

	Notes	2010 US$m	2009 US$m	2008 US$m
Interest income		**58,345**	62,096	91,301
Interest expense		**(18,904)**	(21,366)	(48,738)
Net interest income		**39,441**	40,730	42,563
Fee income		**21,117**	21,403	24,764
Fee expense		**(3,762)**	(3,739)	(4,740)
Net fee income		**17,355**	17,664	20,024
Trading income excluding net interest income		**4,680**	6,236	847
Net interest income on trading activities		**2,530**	3,627	5,713
Net trading income		**7,210**	9,863	6,560
Changes in fair value of long-term debt issued and related derivatives		**(258)**	(6,247)	6,679
Net income/(expense) from other financial instruments designated at fair value		**1,478**	2,716	(2,827)
Net income/(expense) from financial instruments designated at fair value	*3*	**1,220**	(3,531)	3,852
Gains less losses from financial investments		**968**	520	197
Dividend income		**112**	126	272
Net earned insurance premiums	*4*	**11,146**	10,471	10,850
Gains on disposal of French regional banks		**–**	–	2,445
Other operating income		**2,562**	2,788	1,808
Total operating income		**80,014**	78,631	88,571
Net insurance claims incurred and movement in liabilities to policyholders	*5*	**(11,767)**	(12,450)	(6,889)
Net operating income before loan impairment charges and other credit risk provisions		**68,247**	66,181	81,682
Loan impairment charges and other credit risk provisions	*6*	**(14,039)**	(26,488)	(24,937)
Net operating income	*6*	**54,208**	39,693	56,745
Employee compensation and benefits	*7*	**(19,836)**	(18,468)	(20,792)
General and administrative expenses		**(15,156)**	(13,392)	(15,260)
Depreciation and impairment of property, plant and equipment	*25*	**(1,713)**	(1,725)	(1,750)
Goodwill impairment	*24*	**–**	–	(10,564)
Amortisation and impairment of intangible assets	*24*	**(983)**	(810)	(733)
Total operating expenses		**(37,688)**	(34,395)	(49,099)
Operating profit		**16,520**	5,298	7,646
Share of profit in associates and joint ventures	*23*	**2,517**	1,781	1,661
Profit before tax		**19,037**	7,079	9,307
Tax expense	*10*	**(4,846)**	(385)	(2,809)
Profit for the year		**14,191**	6,694	6,498
Profit attributable to shareholders of the parent company		**13,159**	5,834	5,728
Profit attributable to non-controlling interests		**1,032**	860	770
		US$	US$	US$
Basic earnings per ordinary share	*12*	**0.73**	0.34	0.41
Diluted earnings per ordinary share	*12*	**0.72**	0.34	0.41

The accompanying notes on pages 250 to 370, 'Critical accounting policies' on pages 33 to 36, the audited sections of 'Risk' on pages 86 to 176 and the audited sections of 'Capital' on pages 177 to 182 form an integral part of these financial statements.

Consolidated statement of comprehensive income for the year ended 31 December 2010

	2010 US$m	2009 US$m	2008 US$m
Profit for the year	**14,191**	6,694	6,498
Other comprehensive income/(expense)			
Available-for-sale investments	**5,835**	10,817	(21,904)
– fair value gains/(losses)	**6,368**	9,821	(23,722)
– fair value gains transferred to income statement on disposal	**(1,174)**	(648)	(1,316)
– amounts transferred to the income statement in respect of impairment losses	**1,118**	2,391	1,779
– income taxes	**(477)**	(747)	1,355
Cash flow hedges	**(271)**	772	124
– fair value gains/(losses)	**(178)**	481	(1,720)
– fair value (gains)/losses transferred to income statement	**(164)**	808	1,754
– income taxes	**71**	(517)	90
Actuarial losses on defined benefit plans	**(61)**	(2,608)	(1,175)
– before income taxes	**(60)**	(3,586)	(1,609)
– income taxes	**(1)**	978	434
Share of other comprehensive income/(expense) of associates and joint ventures	**107**	149	(559)
Exchange differences	**(567)**	4,975	(12,123)
Other comprehensive income/(expense) for the year, net of tax	**5,043**	14,105	(35,637)
Total comprehensive income/(expense) for the year	**19,234**	20,799	(29,139)
Total comprehensive income/(expense) for the year attributable to:			
– shareholders of the parent company	**18,087**	19,529	(29,143)
– non-controlling interests	**1,147**	1,270	4
	19,234	20,799	(29,139)

The accompanying notes on pages 250 to 370, 'Critical accounting policies' on pages 33 to 36, the audited sections of 'Risk' on pages 86 to 176 and the audited sections of 'Capital' on pages 177 to 182 form an integral part of these financial statements.

Financial Statements (continued)

Consolidated balance sheet / Consolidated statement of cash flows

Consolidated balance sheet at 31 December 2010

	Notes	2010 US$m	2009 US$m
Assets			
Cash and balances at central banks		**57,383**	60,655
Items in the course of collection from other banks		**6,072**	6,395
Hong Kong Government certificates of indebtedness		**19,057**	17,463
Trading assets	*15*	**385,052**	421,381
Financial assets designated at fair value	*19*	**37,011**	37,181
Derivatives	*20*	**260,757**	250,886
Loans and advances to banks		**208,271**	179,781
Loans and advances to customers		**958,366**	896,231
Financial investments	*21*	**400,755**	369,158
Other assets	*27*	**43,251**	44,534
Current tax assets		**1,096**	2,937
Prepayments and accrued income		**11,966**	12,423
Interests in associates and joint ventures	*23*	**17,198**	13,011
Goodwill and intangible assets	*24*	**29,922**	29,994
Property, plant and equipment	*25*	**11,521**	13,802
Deferred tax assets	*10*	**7,011**	8,620
Total assets		**2,454,689**	2,364,452
Liabilities and equity			
Liabilities			
Hong Kong currency notes in circulation		**19,057**	17,463
Deposits by banks		**110,584**	124,872
Customer accounts		**1,227,725**	1,159,034
Items in the course of transmission to other banks		**6,663**	5,734
Trading liabilities	*28*	**300,703**	268,130
Financial liabilities designated at fair value	*29*	**88,133**	80,092
Derivatives	*20*	**258,665**	247,646
Debt securities in issue	*30*	**145,401**	146,896
Other liabilities	*31*	**28,050**	68,640
Current tax liabilities		**1,804**	2,140
Liabilities under insurance contracts	*32*	**58,609**	53,707
Accruals and deferred income		**13,906**	13,190
Provisions	*33*	**2,138**	1,965
Deferred tax liabilities	*10*	**1,093**	1,837
Retirement benefit liabilities	*7*	**3,856**	6,967
Subordinated liabilities	*34*	**33,387**	30,478
Total liabilities		**2,299,774**	2,228,791
Equity			
Called up share capital	*39*	**8,843**	8,705
Share premium account		**8,454**	8,413
Other equity instruments		**5,851**	2,133
Other reserves		**27,169**	22,236
Retained earnings		**97,350**	86,812
Total shareholders' equity		**147,667**	128,299
Non-controlling interests	*38*	**7,248**	7,362
Total equity		**154,915**	135,661
Total equity and liabilities		**2,454,689**	2,364,452

The accompanying notes on pages 250 to 370, 'Critical accounting policies' on pages 33 to 36, the audited sections of 'Risk' on pages 86 to 176 and the audited sections of 'Capital' on pages 177 to 182 form an integral part of these financial statements.

D J Flint, *Group Chairman*

Consolidated statement of cash flows for the year ended 31 December 2010

	Notes	2010 US$m	2009 US$m	2008 US$m
Cash flows from operating activities				
Profit before tax		**19,037**	7,079	9,307
Adjustments for:				
– non-cash items included in profit before tax	*40*	**18,887**	31,384	41,305
– change in operating assets	*40*	**(13,267)**	(20,803)	18,123
– change in operating liabilities	*40*	**42,272**	14,645	(63,413)
– elimination of exchange differences[1]		**(1,799)**	(19,024)	36,132
– net gain from investing activities		**(1,698)**	(1,910)	(4,195)
– share of profits in associates and joint ventures		**(2,517)**	(1,781)	(1,661)
– dividends received from associates		**441**	414	655
– contributions paid to defined benefit plans		**(3,321)**	(974)	(719)
– tax paid		**(2,293)**	(2,132)	(5,114)
Net cash generated from operating activities		**55,742**	6,898	30,420
Cash flows from investing activities				
Purchase of financial investments		**(341,202)**	(304,629)	(277,023)
Proceeds from the sale and maturity of financial investments		**321,846**	241,341	223,138
Purchase of property, plant and equipment		**(2,533)**	(2,000)	(2,985)
Proceeds from the sale of property, plant and equipment		**4,373**	4,701	2,467
Proceeds from the sale of loan portfolios		**4,243**	4,852	9,941
Net purchase of intangible assets		**(1,179)**	(956)	(1,169)
Net cash inflow/(outflow) from acquisition of subsidiaries		**(86)**	(677)	1,313
Net cash inflow from disposal of subsidiaries		**466**	45	2,979
Net cash outflow from acquisition of or increase in stake of associates		**(1,589)**	(62)	(355)
Net cash inflow/(outflow) from the consolidation of funds		**(19,566)**	–	16,500
Proceeds from disposal of associates and joint ventures		**254**	308	101
Net cash used in investing activities		**(34,973)**	(57,077)	(25,093)
Cash flows from financing activities				
Issue of ordinary share capital		**180**	18,398	467
– rights issue		**–**	18,326	–
– other		**180**	72	467
Issue of other equity instruments		**3,718**	–	2,133
Net sales/(purchases) of own shares for market-making and investment purposes		**163**	(176)	(194)
Purchases of own shares to meet share awards and share option awards		**11**	(51)	(808)
On exercise of share options		**2**	12	27
Subordinated loan capital issued		**4,481**	2,959	7,094
Subordinated loan capital repaid		**(2,475)**	(4,637)	(350)
Net cash outflow from change in stake in subsidiaries		**(229)**	–	–
Dividends paid to shareholders of the parent company		**(3,441)**	(4,264)	(7,211)
Dividends paid to non-controlling interests		**(595)**	(702)	(714)
Dividends paid to holders of other equity instruments		**(413)**	(269)	(92)
Net cash generated from financing activities		**1,402**	11,270	352
Net increase/(decrease) in cash and cash equivalents		**22,171**	(38,909)	5,679
Cash and cash equivalents at 1 January		**250,766**	278,872	297,009
Exchange differences in respect of cash and cash equivalents		**1,139**	10,803	(23,816)
Cash and cash equivalents at 31 December	*40*	**274,076**	250,766	278,872

For footnote, see page 249.

The accompanying notes on pages 250 to 370, 'Critical accounting policies' on pages 33 to 36, the audited sections of 'Risk' on pages 86 to 176 and the audited sections of 'Capital' on pages 177 to 182 form an integral part of these financial statements.

Financial Statements (continued)

Consolidated statement of changes in equity

Consolidated statement of changes in equity for the year ended 31 December 2010

	2010											
					Other reserves							
	Called up share capital US$m	Share premium[2] US$m	Other equity instru-ments US$m	Retained earnings[3,4] US$m	Available-for-sale fair value reserve US$m	Cash flow hedging reserve[5] US$m	Foreign exchange reserve US$m	Share-based payment reserve US$m	Merger reserve[3,6] US$m	Total share-holders' equity US$m	Non-controlling interests US$m	Total equity US$m
At 1 January	8,705	8,413	2,133	86,812	(9,965)	(26)	2,994	1,925	27,308	128,299	7,362	135,661
Profit for the year	–	–	–	13,159	–	–	–	–	–	13,159	1,032	14,191
Other comprehensive income (net of tax)	–	–	–	49	5,671	(266)	(526)	–	–	4,928	115	5,043
Available-for-sale investments	–	–	–	–	5,671	–	–	–	–	5,671	164	5,835
Cash flow hedges	–	–	–	–	–	(266)	–	–	–	(266)	(5)	(271)
Actuarial losses on defined benefit plans	–	–	–	(58)	–	–	–	–	–	(58)	(3)	(61)
Share of other comprehensive income of associates and joint ventures	–	–	–	107	–	–	–	–	–	107	–	107
Exchange differences	–	–	–	–	–	–	(526)	–	–	(526)	(41)	(567)
Total comprehensive income for the year	–	–	–	13,208	5,671	(266)	(526)	–	–	18,087	1,147	19,234
Shares issued under employee share plans	12	168	–	–	–	–	–	–	–	180	–	180
Shares issued in lieu of dividends and amounts arising thereon[2]	126	(127)	–	2,524	–	–	–	–	–	2,523	–	2,523
Capital securities issued[7]	–	–	3,718	–	–	–	–	–	–	3,718	–	3,718
Dividends to shareholders	–	–	–	(6,350)	–	–	–	–	–	(6,350)	(725)	(7,075)
Tax credit on dividends	–	–	–	122	–	–	–	–	–	122	–	122
Own shares adjustment	–	–	–	174	–	–	–	–	–	174	–	174
Exercise and lapse of share options and vesting of share awards	–	–	–	809	–	–	–	(809)	–	–	–	–
Cost of share-based payment arrangements	–	–	–	–	–	–	–	812	–	812	–	812
Income taxes on share-based payments	–	–	–	(14)	–	–	–	–	–	(14)	–	(14)
Other movements	–	–	–	(58)	217	7	–	–	–	166	3	169
Transfers	–	–	–	173	–	–	–	(173)	–	–	–	–
Acquisition and disposal of subsidiaries	–	–	–	–	–	–	–	–	–	–	(436)	(436)
Changes in ownership interests in subsidiaries that did not result in loss of control	–	–	–	(50)	–	–	–	–	–	(50)	(103)	(153)
At 31 December	8,843	8,454	5,851	97,350	(4,077)	(285)	2,468	1,755	27,308	147,667	7,248	154,915

	2009											
					Other reserves							
	Called up share capital US$m	Share premium[2] US$m	Other equity instru-ments US$m	Retained earnings[3,4] US$m	Available-for-sale fair value reserve US$m	Cash flow hedging reserve[5] US$m	Foreign exchange reserve US$m	Share-based payment reserve US$m	Merger reserve[3,6] US$m	Total share-holders' equity US$m	Non-controlling interests US$m	Total equity US$m
At 1 January	6,053	8,463	2,133	80,689	(20,550)	(806)	(1,843)	1,995	17,457	93,591	6,638	100,229
Profit for the year	–	–	–	5,834	–	–	–	–	–	5,834	860	6,694
Other comprehensive income (net of tax)	–	–	–	(2,536)	10,603	791	4,837	–	–	13,695	410	14,105
Available-for-sale investments	–	–	–	–	10,603	–	–	–	–	10,603	214	10,817
Cash flow hedges	–	–	–	–	–	791	–	–	–	791	(19)	772
Actuarial gains/(losses) on defined benefit plans	–	–	–	(2,685)	–	–	–	–	–	(2,685)	77	(2,608)
Share of other comprehensive income of associates and joint ventures	–	–	–	149	–	–	–	–	–	149	–	149
Exchange differences	–	–	–	–	–	–	4,837	–	–	4,837	138	4,975
Total comprehensive income for the year	–	–	–	3,298	10,603	791	4,837	–	–	19,529	1,270	20,799
Shares issued under employee share plans	4	69	–	–	–	–	–	–	–	73	–	73
Shares issued in lieu of dividends and amounts arising thereon[2]	118	(119)	–	1,670	–	–	–	–	–	1,669	–	1,669
Shares issued in respect of rights issue[6]	2,530	–	–	–	–	–	–	–	15,796	18,326	–	18,326
Dividends to shareholders	–	–	–	(5,639)	–	–	–	–	–	(5,639)	(832)	(6,471)
Tax credit on dividends	–	–	–	50	–	–	–	–	–	50	–	50
Own shares adjustment	–	–	–	(227)	–	–	–	–	–	(227)	–	(227)
Exercise and lapse of share options and vesting of share awards	–	–	–	807	–	–	–	(769)	–	38	–	38
Cost of share-based payment arrangements	–	–	–	–	–	–	–	683	–	683	–	683
Income taxes on share-based payments	–	–	–	9	–	–	–	–	–	9	–	9
Other movements	–	–	–	210	(18)	(11)	–	16	–	197	77	274
Transfers[6]	–	–	–	5,945	–	–	–	–	(5,945)	–	–	–
Acquisition and disposal of subsidiaries	–	–	–	–	–	–	–	–	–	–	(38)	(38)
Change in ownership interests in subsidiaries that did not result in loss of control	–	–	–	–	–	–	–	–	–	–	247	247
At 31 December	8,705	8,413	2,133	86,812	(9,965)	(26)	2,994	1,925	27,308	128,299	7,362	135,661

Financial Statements (continued)

Consolidated statement of changes in equity / HSBC Holdings balance sheet

Consolidated statement of changes in equity for the year ended 31 December 2010 (continued)

	2008											
					Other reserves							
	Called up share capital US$m	Share premium[2] US$m	Other equity instru-ments US$m	Retained earnings[3,4] US$m	Available-for-sale fair value reserve US$m	Cash flow hedging reserve[5] US$m	Foreign exchange reserve US$m	Share-based payment reserve US$m	Merger reserve[3,6] US$m	Total share-holders' equity US$m	Non-controlling interests US$m	Total equity US$m
At 1 January	5,915	8,134	–	81,097	850	(917)	10,055	1,968	21,058	128,160	7,256	135,416
Profit for the year	–	–	–	5,728	–	–	–	–	–	5,728	770	6,498
Other comprehensive income (net of tax)	–	–	–	(1,605)	(21,474)	106	(11,898)	–	–	(34,871)	(766)	(35,637)
Available-for-sale investments	–	–	–	–	(21,474)	–	–	–	–	(21,474)	(430)	(21,904)
Cash flow hedges	–	–	–	–	–	106	–	–	–	106	18	124
Actuarial gains/(losses) on defined benefit plans	–	–	–	(1,046)	–	–	–	–	–	(1,046)	(129)	(1,175)
Share of other comprehensive income of associates and joint ventures	–	–	–	(559)	–	–	–	–	–	(559)	–	(559)
Exchange differences	–	–	–	–	–	–	(11,898)	–	–	(11,898)	(225)	(12,123)
Total comprehensive income for the year	–	–	–	4,123	(21,474)	106	(11,898)	–	–	(29,143)	4	(29,139)
Shares issued under employee share plans	20	450	–	–	–	–	–	–	–	470	–	470
Shares issued in lieu of dividends and amounts arising thereon[2]	118	(121)	–	3,596	–	–	–	–	–	3,593	–	3,593
Capital securities issued[7]	–	–	2,133	–	–	–	–	–	–	2,133	–	2,133
Dividends to shareholders	–	–	–	(11,301)	–	–	–	–	–	(11,301)	(813)	(12,114)
Own shares adjustment	–	–	–	(1,002)	–	–	–	–	–	(1,002)	–	(1,002)
Exercise and lapse of share options and vesting of share awards	–	–	–	827	–	–	–	(848)	–	(21)	–	(21)
Cost of share-based payment arrangements	–	–	–	–	–	–	–	819	–	819	–	819
Other movements	–	–	–	(252)	74	5	–	56	–	(117)	73	(44)
Transfers[6]	–	–	–	3,601	–	–	–	–	(3,601)	–	–	–
Acquisition and disposal of subsidiaries	–	–	–	–	–	–	–	–	–	–	(33)	(33)
Change in ownership interests in subsidiaries that did not result in loss of control	–	–	–	–	–	–	–	–	–	–	151	151
At 31 December	6,053	8,463	2,133	80,689	(20,550)	(806)	(1,843)	1,995	17,457	93,591	6,638	100,229

Dividends per ordinary share at 31 December 2010 were US$0.34 (2009: US$0.34; 2008: US$0.93).

For footnotes, see page 249.

The accompanying notes on pages 250 to 370, 'Critical accounting policies' on pages 33 to 36, the audited sections of 'Risk' on pages 86 to 176 and the audited sections of 'Capital' on pages 177 to 182 form an integral part of these financial statements.

HSBC Holdings balance sheet at 31 December 2010

	Notes	2010 US$m	2009 US$m
Assets			
Cash at bank and in hand:			
– balances with HSBC undertakings		**459**	224
Derivatives	*20*	**2,327**	2,981
Loans and advances to HSBC undertakings		**21,238**	23,212
Financial investments		**2,025**	2,455
Other assets		**1**	4
Current tax assets		**224**	562
Prepayments and accrued income		**107**	102
Investments in subsidiaries	*26*	**92,899**	86,247
Property, plant and equipment		**4**	6
Deferred tax assets	*10*	**57**	–
Total assets		**119,341**	115,793
Liabilities and equity			
Liabilities			
Amounts owed to HSBC undertakings		**2,932**	3,711
Financial liabilities designated at fair value	*29*	**16,288**	16,909
Derivatives	*20*	**827**	362
Debt securities in issue	*30*	**2,668**	2,839
Other liabilities	*31*	**1,232**	1,257
Accruals and deferred income		**750**	419
Deferred tax liabilities	*10*	**–**	14
Subordinated liabilities	*34*	**13,313**	14,406
Total liabilities		**38,010**	39,917
Equity			
Called up share capital	*39*	**8,843**	8,705
Share premium account		**8,454**	8,413
Other equity instruments		**5,828**	2,133
Merger reserve and other reserves		**35,127**	35,127
Other reserves		**3,394**	3,642
Retained earnings		**19,685**	17,856
Total equity		**81,331**	75,876
Total equity and liabilities		**119,341**	115,793

The accompanying notes on pages 250 to 370, 'Critical accounting policies' on pages 33 to 36, the audited sections of 'Risk' on pages 86 to 176 and the audited sections of 'Capital' on pages 177 to 182 form an integral part of these financial statements.

D J Flint, *Group Chairman*

Financial Statements (continued)

HSBC Holdings statement of cash flows for the year ended 31 December 2010

	Notes	2010 US$m	2009 US$m
Cash flows from operating activities			
Profit/(loss) before tax		**5,237**	(2,058)
Adjustments for:			
– non-cash items included in profit before tax	*40*	**185**	5,974
– change in operating assets	*40*	**3,091**	(11,077)
– change in operating liabilities	*40*	**(1,754)**	2,040
– elimination of exchange differences[1]		**–**	1
– tax received		**853**	266
Net cash generated from/(used in) operating activities		**7,612**	(4,854)
Cash flows from investing activities			
Proceeds from sale of financial investments		**–**	275
Purchase of property, plant and equipment		**–**	(2)
Net cash outflow from acquisition of or increase in stake of subsidiaries		**(6,649)**	(10,344)
Net cash used in investing activities		**(6,649)**	(10,071)
Cash flows from financing activities			
Issue of ordinary share capital		**180**	18,333
– rights issue		**–**	18,261
– other		**180**	72
Issue of other equity instruments		**3,695**	–
On exercise of share options		**2**	12
Subordinated loan capital issued		**1,349**	2,456
Subordinated loan capital repaid		**(2,100)**	(4,380)
Debt securities issued		**–**	2,818
Dividends paid		**(3,441)**	(4,264)
Dividends paid to holders of other equity instruments		**(413)**	(269)
Net cash (used in)/generated from financing activities		**(728)**	14,706
Net increase/(decrease) in cash and cash equivalents		**235**	(219)
Cash and cash equivalents at 1 January		**224**	443
Cash and cash equivalents at 31 December	*40*	**459**	224

For footnote, see page 249.

The accompanying notes on pages 250 to 370, 'Critical accounting policies' on pages 33 to 36, the audited sections of 'Risk' on pages 86 to 176 and the audited sections of 'Capital' on pages 177 to 182 form an integral part of these financial statements.

HSBC Holdings statement of changes in equity for the year ended 31 December 2010

	2010								
					Other reserves				
	Called up share capital US$m	Share premium[2] US$m	Other equity instru-ments[7] US$m	Retained earnings[8] US$m	Available-for-sale fair value reserve US$m	Other paid-in capital US$m	Share-based payment reserve US$m	Merger and other reserves[6] US$m	Total share-holders' equity US$m
At 1 January	8,705	8,413	2,133	17,856	253	1,464	1,925	35,127	75,876
Profit for the year	–	–	–	5,658	–	–	–	–	5,658
Other comprehensive income (net of tax)	–	–	–	–	(197)	–	–	–	(197)
Available-for-sale investments	–	–	–	–	(275)	–	–	–	(275)
Income tax	–	–	–	–	78	–	–	–	78
Total comprehensive income for the year	–	–	–	5,658	(197)	–	–	–	5,461
Shares issued under employee share plans	12	168	–	–	–	–	–	–	180
Shares issued in lieu of dividends and amounts arising thereon[2]	126	(127)	–	2,524	–	–	–	–	2,523
Capital securities issued[7]	–	–	3,695	–	–	–	–	–	3,695
Dividends to shareholders	–	–	–	(6,350)	–	–	–	–	(6,350)
Own shares adjustment	–	–	–	(260)	–	–	–	–	(260)
Exercise and lapse of share options and vesting of share awards	–	–	–	–	–	119	(119)	–	–
Cost of share-based payment arrangements	–	–	–	–	–	–	28	–	28
Equity investments granted to employees of subsidiaries under employee share plans	–	–	–	–	–	–	76	–	76
Other movements	–	–	–	87	–	–	15	–	102
Transfers	–	–	–	170	–	–	(170)	–	–
At 31 December	8,843	8,454	5,828	19,685	56	1,583	1,755	35,127	81,331

Financial Statements (continued)

HSBC Holdings statement of changes in equity for the year ended 31 December 2010 (continued)

	2009								
					Other reserves				
	Called up share capital US$m	Share premium[2] US$m	Other equity instru-ments US$m	Retained earnings[8] US$m	Available-for-sale fair value reserve US$m	Other paid-in capital US$m	Share-based payment reserve US$m	Merger and other reserves[6] US$m	Total share-holders' equity US$m
At 1 January	6,053	8,463	2,133	17,094	190	1,318	1,995	25,341	62,587
Profit for the year	–	–	–	(1,096)	–	–	–	–	(1,096)
Other comprehensive income (net of tax)	–	–	–	–	63	–	–	–	63
Available-for-sale investments	–	–	–	–	103	–	–	–	103
Income tax	–	–	–	–	(40)	–	–	–	(40)
Total comprehensive income for the year	–	–	–	(1,096)	63	–	–	–	(1,033)
Shares issued under employee share plans	4	69	–	–	–	–	–	–	73
Shares issued in lieu of dividends and amounts arising thereon[2]	118	(119)	–	1,670	–	–	–	–	1,669
Shares issued in respect of rights issue	2,530	–	–	–	–	–	–	15,731	18,261
Dividends to shareholders	–	–	–	(5,639)	–	–	–	–	(5,639)
Own shares adjustment	–	–	–	(188)	–	–	–	–	(188)
Exercise and lapse of share options and vesting of share awards	–	–	–	–	–	146	(146)	–	–
Cost of share-based payment arrangements	–	–	–	–	–	–	163	–	163
Income taxes on share-based payments	–	–	–	19	–	–	–	–	19
Equity investments granted to employees of subsidiaries under employee share plans	–	–	–	–	–	–	(99)	–	(99)
Other movements	–	–	–	51	–	–	12	–	63
Transfers[6]	–	–	–	5,945	–	–	–	(5,945)	–
At 31 December	8,705	8,413	2,133	17,856	253	1,464	1,925	35,127	75,876

Dividends per ordinary share at 31 December 2010 were US$0.34 (2009: US$0.34; 2008: US$0.93).

For footnotes, see page 249.

The accompanying notes on pages 250 to 370, 'Critical accounting policies' on pages 33 to 36, the audited sections of 'Risk' on pages 86 to 176 and the audited sections of 'Capital' on pages 177 to 182 form an integral part of these financial statements.

Footnotes to Financial Statements

1 *Adjustment to bring changes between opening and closing balance sheet amounts to average rates. This is not done on a line-by-line basis, as details cannot be determined without unreasonable expense.*
2 *Share premium includes the deduction of US$1m in respect of issuance costs incurred during the year (2009: US$1m; 2008: US$3m).*
3 *Cumulative goodwill amounting to US$5,138m has been charged against reserves in respect of acquisitions of subsidiaries prior to 1 January 1998, including US$3,469m charged against the merger reserve arising on the acquisition of HSBC Bank plc. The balance of US$1,669m has been charged against retained earnings.*
4 *Retained earnings include 123,331,979 (US$1,799m) of own shares held within HSBC's insurance business, retirement funds for the benefit of policyholders or beneficiaries within employee trusts for the settlement of shares expected to be delivered under employee share schemes or bonus plans, and the market-making activities in Global Markets (2009: 179,964,968 (US$2,572m); 2008: 194,751,829 (US$3,094m)).*
5 *Amounts transferred to the income statement in respect of cash flow hedges include US$605m (2009: US$502m; 2008: US$152m) taken to 'Net interest income' and US$441m (2009: US$306m; 2008: US$1,602m) taken to 'Net trading income'.*
6 *Statutory share premium relief under Section 131 of the Companies Act 1985 (the 'Act') was taken in respect of the acquisition of HSBC Bank plc in 1992, HSBC France in 2000 and HSBC Finance Corporation in 2003 and the shares issued were recorded at their nominal value only. In HSBC's consolidated financial statements the fair value differences of US$8,290m in respect of HSBC France and US$12,768m in respect of HSBC Finance Corporation were recognised in the merger reserve. The merger reserve created on the acquisition of HSBC Finance Corporation subsequently became attached to HSBC Overseas Holdings (UK) Limited ('HOHU'), following a number of intra-group reorganisations. At 31 December 2009, US$5,945m (2010: nil) was transferred from this reserve to retained earnings as a result of impairment in HSBC Holdings' investment in HOHU. During 2009, pursuant to section 131 of the Companies Act 1985, statutory share premium relief was taken in respect of the rights issue and US$15,796m was recognised in the merger reserve. The merger reserve includes the deduction of US$614m in respect of costs relating to the rights issue, of which US$149m was subsequently transferred to the income statement. Of this US$149m, US$121m was a loss arising from accounting for the agreement with the underwriters as a contingent forward contract. The merger reserve excludes the loss of US$344m on a forward foreign exchange contract associated with hedging the proceeds of the rights issue.*
7 *During June 2010, HSBC Holdings issued US$3,800m of Perpetual Subordinated Capital Securities, Series 2 ('capital securities'), on which there were US$82m of external issuance costs and US$23m of intra-group issuance costs which are classified as equity under IFRSs. In April 2008, HSBC Holdings issued US$2,200m of Perpetual Subordinated Capital Securities, including US$67m of issuance costs, which are classified as equity under IFRSs.*
8 *Retained earnings include 39,814,107 (US$562m) of own shares held to fund employee share plans (2009: 38,446,053 (US$562m)).*

1 Basis of preparation

(a) Compliance with International Financial Reporting Standards

The consolidated financial statements of HSBC and the separate financial statements of HSBC Holdings have been prepared in accordance with International Financial Reporting Standards ('IFRSs') as issued by the International Accounting Standards Board ('IASB') and as endorsed by the EU. EU-endorsed IFRSs may differ from IFRSs as issued by the IASB if, at any point in time, new or amended IFRSs have not been endorsed by the EU. At 31 December 2010, there were no unendorsed standards effective for the year ended 31 December 2010 affecting these consolidated and separate financial statements, and there was no difference between IFRSs endorsed by the EU and IFRSs issued by the IASB in terms of their application to HSBC. Accordingly, HSBC's financial statements for the year ended 31 December 2010 are prepared in accordance with IFRSs as issued by the IASB.

IFRSs comprise accounting standards issued by the IASB and its predecessor body as well as interpretations issued by the IFRS Interpretations Committee ('IFRIC') and its predecessor body.

During 2010, HSBC adopted the following major revisions and amendments to standards:

HSBC adopted the revised IFRS 3 'Business Combinations' ('IFRS 3') and amendments to IAS 27 'Consolidated and Separate Financial Statements' ('IAS 27'). The main changes under the standards are that:

– acquisition-related costs are recognised as an expense in the income statement in the period in which they are incurred;
– all consideration transferred, including contingent consideration, is recognised and measured at fair value at the acquisition date;
– equity interests held prior to control being obtained are remeasured to fair value at the date of obtaining control, and any gain or loss is recognised in the income statement;
– an option is available, on a transaction-by-transaction basis, to measure any non-controlling (previously referred to as minority) interests in the entity acquired either at fair value, or at the non-controlling interests' proportionate share of the net identifiable assets of the entity acquired; and
– changes in a parent's ownership interest in a subsidiary that do not result in a change of control are treated as transactions between equity holders and are reported in equity.

In terms of their application to HSBC, the revised IFRS 3 and the amendments to IAS 27 apply prospectively to acquisitions and transactions taking place on or after 1 January 2010, and have had no significant effect on the consolidated financial statements of HSBC and the separate financial statements of HSBC Holdings.

During 2010, in addition to the above, HSBC adopted a number of interpretations and amendments to standards which had an insignificant effect on the consolidated financial statements of HSBC and the separate financial statements of HSBC Holdings.

(b) Differences between IFRSs and Hong Kong Financial Reporting Standards

There are no significant differences between IFRSs and Hong Kong Financial Reporting Standards in terms of their application to HSBC and consequently there would be no significant differences had the financial statements been prepared in accordance with Hong Kong Financial Reporting Standards. The Notes on the Financial Statements, taken together with the Report of the Directors, include the aggregate of all disclosures necessary to satisfy IFRSs and Hong Kong reporting requirements.

(c) Presentation of information

Disclosures under IFRS 4 'Insurance Contracts' ('IFRS 4') and IFRS 7 'Financial Instruments: Disclosures' ('IFRS 7') concerning the nature and extent of risks relating to insurance contracts and financial instruments have been included in the audited sections of the 'Report of the Directors: Risk' on pages 86 to 176.

Capital disclosures under IAS 1 'Presentation of Financial Statements' ('IAS 1') have been included in the audited sections of 'Report of the Directors: Capital' on pages 177 to 182.

Disclosures relating to HSBC's securitisation activities and structured products have been included in the audited section of 'Report of the Directors: Risk' on pages 86 to 176.

In accordance with HSBC's policy to provide meaningful disclosures that help investors and other stakeholders understand the Group's performance, financial position and changes thereto, the information provided in the Notes on the Financial Statements and the Report of the Directors goes beyond the minimum levels required by accounting standards, statutory and regulatory requirements and listing rules. In particular, HSBC has adopted the British Bankers' Association Code for Financial Reporting Disclosure ('the BBA Code'). The BBA Code aims to increase the quality and comparability of banks' disclosures and sets out five disclosure principles together with supporting guidance. In line with the principles of the BBA Code, HSBC assesses good practice recommendations issued from time to time by relevant regulators and standard setters and will assess the applicability and relevance of such guidance, enhancing disclosures where appropriate.

In publishing the parent company financial statements here together with the Group financial statements, HSBC Holdings has taken advantage of the exemption in section 408(3) of the Companies Act 2006 not to present its individual income statement and related notes that form a part of these financial statements.

HSBC's consolidated financial statements are presented in US dollars which is also HSBC Holdings' functional currency. HSBC Holdings' functional currency is the US dollar because the US dollar and currencies linked to it are the most significant currencies relevant to the underlying transactions, events and conditions of its subsidiaries, as well as representing a significant proportion of its funds generated from financing activities. HSBC uses the US dollar as its presentation currency in its consolidated financial statements because the US dollar and currencies linked to it form the major currency bloc in which HSBC transacts and funds its business.

(d) Comparative information

As required by US public company reporting requirements, these consolidated financial statements include two years of comparative information for the consolidated income statement, consolidated statement of comprehensive income, consolidated statement of cash flows, consolidated statement of changes in equity and related Notes on the Financial Statements.

(e) Use of estimates and assumptions

The preparation of financial information requires the use of estimates and assumptions about future conditions. The use of available information and the application of judgement are inherent in the formation of estimates; actual results in the future may differ from estimates upon which financial information is prepared. Management believes that HSBC's critical accounting policies where judgement is necessarily applied are those which relate to impairment of loans and advances, goodwill impairment, the valuation of financial instruments, the impairment of available-for-sale financial assets and deferred tax assets (see 'Critical Accounting Policies' on pages 33 to 36, which form an integral part of these financial statements).

Further information about key assumptions concerning the future, and other key sources of estimation uncertainty, are set out in the Notes on the Financial Statements.

(f) Consolidation

The consolidated financial statements of HSBC comprise the financial statements of HSBC Holdings and its subsidiaries made up to 31 December, with the exception of the banking and insurance subsidiaries of HSBC Bank Argentina, whose financial statements are made up to 30 June annually to comply with local regulations. Accordingly, HSBC uses their audited interim financial statements, drawn up to 31 December annually.

Subsidiaries are consolidated from the date that HSBC gains control. The acquisition method of accounting is used when subsidiaries are acquired by HSBC. The cost of an acquisition is measured at the fair value of the consideration, including contingent consideration, given at the date of exchange. Acquisition-related costs are recognised as an expense in the income statement in the period in which they are incurred. The acquired identifiable assets, liabilities and contingent liabilities are measured at their fair values at the date of acquisition. Goodwill is measured as the excess of the aggregate of the consideration transferred, the amount of non-controlling interest and the fair value of HSBC's previously held equity interest, if any, over the net of the amounts of the identifiable assets acquired and the liabilities assumed. The amount of non-controlling interest is measured either at fair value or at the non-controlling interest's proportionate share of the acquiree's identifiable net assets. In a business combination achieved in stages, the previously held equity interest is remeasured at the acquisition-date fair value with the resulting gain or loss recognised in the income statement. In the event that the amounts of net assets acquired is in excess of the aggregate of the consideration transferred, the amount of non-controlling interest and the fair value of HSBC's previously held equity interest, the difference is recognised immediately in the income statement.

Changes in a parent's ownership interest in a subsidiary that do not result in a loss of control are treated as transactions between equity holders and are reported in equity.

Entities that are controlled by HSBC are consolidated until the date that control ceases.

In the context of Special Purpose Entities ('SPE's), the following circumstances may indicate a relationship in which, in substance, HSBC controls and consequently consolidates an SPE:

– the activities of the SPE are being conducted on behalf of HSBC according to its specific business needs so that HSBC obtains benefits from the SPE's operation;
– HSBC has the decision-making powers to obtain the majority of the benefits of the activities of the SPE or, by setting up an 'autopilot' mechanism, HSBC has delegated these decision-making powers;
– HSBC has rights to obtain the majority of the benefits of the SPE and therefore may be exposed to risks incidental to the activities of the SPE; or
– HSBC retains the majority of the residual or ownership risks related to the SPE or its assets in order to obtain benefits from its activities.

HSBC performs a re-assessment of consolidation whenever there is a change in the substance of the relationship between HSBC and an SPE.

All intra-HSBC transactions are eliminated on consolidation.

The consolidated financial statements of HSBC also include the attributable share of the results and reserves of joint ventures and associates. These are based on financial statements made up to 31 December, with the exception of the Bank of Communications, Ping An Insurance and Industrial Bank which are included on the basis of financial statements made up for the twelve months to 30 September. These are equity accounted three months in arrears in order to meet the requirements of the Group's reporting timetable. HSBC has taken into account the effect of significant transactions or events that occur between the period from 1 October to 31 December that would have a material effect on its results.

(g) Future accounting developments

At 31 December 2010, a number of standards and interpretations, and amendments thereto, had been issued by the IASB, which are not effective for HSBC's consolidated financial statements or the separate financial statements of HSBC Holdings as at 31 December 2010. Those which are expected to have a significant effect on HSBC's consolidated financial statements and the separate financial statements of HSBC Holdings are discussed below.

Standards and Interpretations issued by the IASB but not endorsed by the EU

In November 2009, the IASB issued IFRS 9 'Financial Instruments' ('IFRS 9') which introduced new requirements for the classification and measurement of financial assets. In October 2010, the IASB issued additions to IFRS 9 relating to financial liabilities. Together, these changes represent the first phase in the IASB's planned replacement of IAS 39 'Financial Instruments: Recognition and Measurement' ('IAS 39') with a less complex and improved standard for financial instruments.

The standard is effective for annual periods beginning on or after 1 January 2013 with early adoption permitted. IFRS 9 is required to be applied retrospectively. If the standard is adopted prior to 1 January 2012, an entity will be exempt from the requirement to restate prior period comparative information. IFRS 9 is subject to EU endorsement, the timing of which is uncertain. Accordingly, HSBC is unable to provide a date by which it plans to apply IFRS 9.

The main changes to the requirements of IAS 39 are summarised below.

- All financial assets that are currently in the scope of IAS 39 will be classified as either amortised cost or fair value. The available-for-sale, held-to-maturity and loans and receivables categories will no longer exist.
- Classification of financial assets is based on an entity's business model for managing the financial assets and their contractual cash flow characteristics. Reclassifications between the two categories are prohibited unless there is a change in the entity's business model.
- A financial asset is measured at amortised cost if two criteria are met: i) the objective of the business model is to hold the financial asset for the collection of the contractual cash flows; and ii) the contractual cash flows of the instrument are solely payments of principal and interest on the principal outstanding. All other financial assets are measured at fair value. Movements in the fair value of financial assets classified at fair value are recognised in profit or loss, except for equity investments where an entity takes the option to designate an equity instrument that is not held for trading at fair value through other comprehensive income. If this option is taken, all subsequent changes in fair value are recognised in other comprehensive income with no recycling of gains or losses to the income statement. Dividend income would continue to be recognised in the income statement.
- An entity is only permitted to designate a financial asset otherwise meeting the amortised cost criteria at fair value through profit or loss if doing so significantly reduces or eliminates an accounting mismatch. This designation is made on initial recognition and is irrevocable.
- Financial assets which contain embedded derivatives are to be classified in their entirety either at fair value or amortised cost depending on whether the contracts as a whole meet the relevant criteria under IFRS 9.
- Most of IAS 39's requirements for financial liabilities are retained, including amortised cost accounting for most financial liabilities. The guidance on separation of embedded derivatives will continue to apply to host contracts that are financial liabilities. However, fair value changes attributable to changes in own credit risk for financial liabilities designated under the fair value option other than loan commitments and financial guarantee contracts are to be presented in the statement of other comprehensive income unless the treatment would create or enlarge an accounting mismatch in profit or loss. These amounts are not subsequently reclassified to the income statement but may be transferred within equity.

The second and third phases in the IASB's project to replace IAS 39 will address the impairment of financial assets measured at amortised cost and hedge accounting. The IASB has indicated that it expects to finalise the replacement of IAS 39 by June 2011. In addition, the IASB is working with the US Financial Accounting Standards Board to reduce inconsistencies between US GAAP and IFRS in accounting for financial instruments. The impact of IFRS 9 may change as a consequence of further developments resulting from the IASB's project to replace IAS 39. As a result, it is impracticable to quantify the impact of IFRS 9 as at the date of publication of these financial statements.

2 Summary of significant accounting policies

(a) Interest income and expense

Interest income and expense for all financial instruments except for those classified as held for trading or designated at fair value (other than debt securities issued by HSBC and derivatives managed in conjunction with such debt securities issued) are recognised in 'Interest income' and 'Interest expense' in the income statement using the effective interest method. The effective interest method is a way of calculating the amortised cost of a financial asset or a financial liability (or groups of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period.

The effective interest rate is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, HSBC estimates cash flows considering all contractual terms of the financial instrument but excluding future credit losses. The calculation includes all amounts paid or received by HSBC that are an integral part of the effective interest rate of a financial instrument, including transaction costs and all other premiums or discounts.

Interest on impaired financial assets is recognised using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss.

(b) Non-interest income

Fee income is earned from a diverse range of services provided by HSBC to its customers. Fee income is accounted for as follows:

- income earned on the execution of a significant act is recognised as revenue when the act is completed (for example, fees arising from negotiating, or participating in the negotiation of, a transaction for a third-party, such as an arrangement for the acquisition of shares or other securities);
- income earned from the provision of services is recognised as revenue as the services are provided (for example, asset management, portfolio and other management advisory and service fees); and
- income which forms an integral part of the effective interest rate of a financial instrument is recognised as an adjustment to the effective interest rate (for example, certain loan commitment fees) and recorded in 'Interest income' (Note 2a).

Net trading income comprises all gains and losses from changes in the fair value of financial assets and financial liabilities held for trading, together with the related interest income, expense and dividends.

Net income from financial instruments designated at fair value includes all gains and losses from changes in the fair value of financial assets and financial liabilities designated at fair value through profit or loss. Interest income and expense and dividend income arising on these financial instruments are also included, except for interest arising from debt securities issued, and derivatives managed in conjunction with those debt securities, which is recognised in 'Interest expense' (Note 2a).

Dividend income is recognised when the right to receive payment is established. This is the ex-dividend date for listed equity securities, and usually the date when shareholders have approved the dividend for unlisted equity securities.

(c) Operating segments

HSBC's operating segments are organised into six geographical regions; Europe, Hong Kong, Rest of Asia-Pacific, Middle East, North America and Latin America. Due to the nature of the Group, HSBC's chief operating decision-maker regularly reviews operating activity on a number of bases, including by geographical region, customer group and global business, and retail businesses by geographical region. HSBC's operating segments were determined to be geographical regions because the chief operating decision-maker primarily uses information on geographical regions in order to make decisions about allocating resources and assessing performance.

Measurement of segmental assets, liabilities, income and expenses is in accordance with the Group's accounting policies. Segmental income and expenses include transfers between segments and these transfers are conducted on arm's length terms and conditions. Shared costs are included in segments on the basis of the actual recharges made.

(d) Valuation of financial instruments

All financial instruments are recognised initially at fair value. In the normal course of business, the fair value of a financial instrument on initial recognition is the transaction price (that is, the fair value of the consideration given or received). In certain circumstances, however, the fair value will be based on other observable current market transactions in the same instrument, without modification or repackaging, or on a valuation technique whose variables include only data from observable markets, such as interest rate yield curves, option volatilities and currency rates. When such evidence exists, HSBC recognises a trading gain or loss on inception of the financial instrument, being the difference between the transaction price and the fair value. When unobservable market data have a significant impact on the valuation of financial instruments, the entire initial difference in fair value indicated by the valuation model from the transaction price is not recognised immediately in the income statement but is recognised over the life of the transaction on an appropriate basis, or when the inputs become observable, or the transaction matures or is closed out, or when HSBC enters into an offsetting transaction.

Subsequent to initial recognition, the fair values of financial instruments measured at fair value are measured in accordance with HSBC's valuation methodologies, which are described in Note 16.

(e) Reclassification of financial assets

Non-derivative financial assets (other than those designated at fair value through profit or loss upon initial recognition) may be reclassified out of the fair value through profit or loss category in the following circumstances:

- financial assets that would have met the definition of loans and receivables at initial recognition (if the financial asset had not been required to be classified as held for trading) may be reclassified out of the fair value through profit or loss category if there is the intention and ability to hold the financial asset for the foreseeable future or until maturity; and
- financial assets (except financial assets that would have met the definition of loans and receivables at initial recognition) may be reclassified out of the fair value through profit or loss category and into another category in rare circumstances.

When a financial asset is reclassified as described in the above circumstances, the financial asset is reclassified at its fair value on the date of reclassification. Any gain or loss already recognised in the income statement is not reversed. The fair value of the financial asset on the date of reclassification becomes its new cost or amortised cost, as applicable.

(f) Loans and advances to banks and customers

Loans and advances to banks and customers include loans and advances originated by HSBC which are not classified either as held for trading or designated at fair value. Loans and advances are recognised when cash is advanced to a borrower. They are derecognised when either the borrower repays its obligations, or the loans are sold or written off, or substantially all the risks and rewards of ownership are transferred. They are initially recorded at fair value plus any directly attributable transaction costs and are subsequently measured at amortised cost using the effective interest method, less any impairment losses. Where exposures are hedged by derivatives designated and qualifying as fair value hedges, the carrying value of the loans and advances so hedged includes a fair value adjustment for the hedged risk only.

HSBC may commit to underwrite loans on fixed contractual terms for specified periods of time, where the drawdown of the loan is contingent upon certain future events outside the control of HSBC. Where the loan arising from the lending commitment is expected to be held for trading, the commitment to lend is recorded as a derivative and measured at fair value through profit or loss. On drawdown, the loan is classified as held for trading and measured at fair value through profit or loss. Where it is not HSBC's intention to trade but hold the loan, a provision on the loan commitment is only recorded where it is probable that HSBC will incur a loss. This may occur, for example, where a loss of principal is probable or the interest rate charged on the loan is lower than the cost of funding. On inception of the loan, the loan to be held is recorded at its fair value and subsequently measured at amortised cost using the effective interest method. For certain transactions, such as leveraged finance and syndicated lending activities, the cash advanced is not necessarily the best evidence of the fair value of the loan. For these loans, where the initial fair value is lower than the cash amount advanced (for example, due to the rate of interest charged on the loan being below the market rate of interest), the write-down is charged to the income statement. The write-down will be recovered over the life of the loan, through the recognition of interest income using the effective interest method, unless the loan becomes impaired. The write-down is recorded as a reduction to other operating income.

Financial assets which have been reclassified into the loans and receivables category are initially recorded at the fair value at the date of reclassification and are subsequently measured at amortised cost, using the effective interest rate determined at the date of reclassification.

(g) Impairment of loans and advances

Losses for impaired loans are recognised promptly when there is objective evidence that impairment of a loan or portfolio of loans has occurred. Impairment allowances are calculated on individual loans and on groups of loans assessed collectively. Impairment losses are recorded as charges to the income statement. The carrying amount of impaired loans on the balance sheet is reduced through the use of impairment allowance accounts. Losses expected from future events are not recognised.

Individually assessed loans and advances

For all loans that are considered individually significant, HSBC assesses on a case-by-case basis at each balance sheet date whether there is any objective evidence that a loan is impaired. The criteria used by HSBC to determine that there is such objective evidence include:

– known cash flow difficulties experienced by the borrower;
– past due contractual payments of either principal or interest;
– breach of loan covenants or conditions;
– the probability that the borrower will enter bankruptcy or other financial realisation; and
– a significant downgrading in credit rating by an external credit rating agency.

For those loans where objective evidence of impairment exists, impairment losses are determined considering the following factors:

– HSBC's aggregate exposure to the customer;
– the viability of the customer's business model and their capacity to trade successfully out of financial difficulties and generate sufficient cash flow to service debt obligations;
– the amount and timing of expected receipts and recoveries;
– the likely dividend available on liquidation or bankruptcy;
– the extent of other creditors' commitments ranking ahead of, or *pari passu* with, HSBC and the likelihood of other creditors continuing to support the company;
– the complexity of determining the aggregate amount and ranking of all creditor claims and the extent to which legal and insurance uncertainties are evident;
– the realisable value of security (or other credit mitigants) and likelihood of successful repossession;
– the likely deduction of any costs involved in recovery of amounts outstanding;
– the ability of the borrower to obtain, and make payments in, the currency of the loan if not denominated in local currency; and
– when available, the secondary market price of the debt.

Impairment losses are calculated by discounting the expected future cash flows of a loan at its original effective interest rate and comparing the resultant present value with the loan's current carrying amount. The impairment allowances on individually significant accounts are reviewed at least quarterly and more regularly when circumstances require. This normally encompasses re-assessment of the enforceability of any collateral held and the timing and amount of actual and anticipated receipts. Individually assessed impairment allowances are only released when there is reasonable and objective evidence of a reduction in the established loss estimate.

Collectively assessed loans and advances

Impairment is assessed on a collective basis in two circumstances:

– to cover losses which have been incurred but have not yet been identified on loans subject to individual assessment; and
– for homogeneous groups of loans that are not considered individually significant.

Incurred but not yet identified impairment

Individually assessed loans for which no evidence of loss has been specifically identified on an individual basis are grouped together according to their credit risk characteristics for the purpose of calculating an estimated collective loss. This reflects impairment losses that HSBC has incurred as a result of events occurring before the balance sheet date, which HSBC is not able to identify on an individual loan basis, and that can be reliably estimated. These losses will only be individually identified in the future. As soon as information becomes available which identifies losses on individual loans within the group, those loans are removed from the group and assessed on an individual basis for impairment.

The collective impairment allowance is determined after taking into account:

- historical loss experience in portfolios of similar credit risk characteristics (for example, by industry sector, loan grade or product);
- the estimated period between impairment occurring and the loss being identified and evidenced by the establishment of an appropriate allowance against the individual loan; and
- management's experienced judgement as to whether current economic and credit conditions are such that the actual level of inherent losses at the balance sheet date is likely to be greater or less than that suggested by historical experience.

The period between a loss occurring and its identification is estimated by local management for each identified portfolio.

Homogeneous groups of loans and advances

Statistical methods are used to determine impairment losses on a collective basis for homogeneous groups of loans that are not considered individually significant, because individual loan assessment is impracticable. Losses in these groups of loans are recorded on an individual basis when individual loans are written off, at which point they are removed from the group. Two alternative methods are used to calculate allowances on a collective basis:

- When appropriate empirical information is available, HSBC utilises roll rate methodology. This methodology employs statistical analyses of historical data and experience of delinquency and default to estimate the amount of loans that will eventually be written off as a result of the events occurring before the balance sheet date which HSBC is not able to identify on an individual loan basis, and that can be reliably estimated. Under this methodology, loans are grouped into ranges according to the number of days past due and statistical analysis is used to estimate the likelihood that loans in each range will progress through the various stages of delinquency, and ultimately prove irrecoverable. Current economic conditions are also evaluated when calculating the appropriate level of allowance required to cover inherent loss. The estimated loss is the difference between the present value of expected future cash flows, discounted at the original effective interest rate of the portfolio, and the carrying amount of the portfolio. In certain highly developed markets, sophisticated models also take into account behavioural and account management trends as revealed in, for example, bankruptcy and rescheduling statistics.
- When the portfolio size is small or when information is insufficient or not reliable enough to adopt a roll rate methodology, HSBC adopts a basic formulaic approach based on historical loss rate experience.

In normal circumstances, historical experience provides the most objective and relevant information from which to assess inherent loss within each portfolio, though sometimes it provides less relevant information about the inherent loss in a given portfolio at the balance sheet date, for example, when there have been changes in economic, regulatory or behavioural conditions which result in the most recent trends in portfolio risk factors being not fully reflected in the statistical models. In these circumstances, the risk factors are taken into account by adjusting the impairment allowances derived solely from historical loss experience.

These additional portfolio risk factors may include recent loan portfolio growth and product mix, unemployment rates, bankruptcy trends, geographic concentrations, loan product features (such as the ability of borrowers to repay adjustable-rate loans where reset interest rates give rise to increases in interest charges), economic conditions such as national and local trends in housing markets and interest rates, portfolio seasoning, account management policies and practices, current levels of write-offs, changes in laws and regulations and other items which can affect customer payment patterns on outstanding loans, such as natural disasters. These risk factors, where relevant, are taken into account when calculating the appropriate level of impairment allowances by adjusting the impairment allowances derived solely from historical loss experience.

Roll rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure they remain appropriate.

Write-off of loans and advances

Loans (and the related impairment allowance accounts) are normally written off, either partially or in full, when there is no realistic prospect of recovery. Where loans are secured, this is generally after receipt of any proceeds from the realisation of security. In circumstances where the net realisable value of any collateral has been determined and there is no reasonable expectation of further recovery, write off may be earlier.

Reversals of impairment

If the amount of an impairment loss decreases in a subsequent period, and the decrease can be related objectively to an event occurring after the impairment was recognised, the excess is written back by reducing the loan impairment allowance account accordingly. The write-back is recognised in the income statement.

Reclassified loans and advances

Where financial assets have been reclassified out of the fair value through profit or loss category to the loans and receivables category, the effective interest rate determined at the date of reclassification is used to calculate any impairment losses.

Following reclassification, where there is a subsequent increase in the estimates of future cash receipts as a result of increased recoverability of those cash receipts, the effect of that increase is recognised as an adjustment to the effective interest rate from the date of change in the estimate rather than as an adjustment to the carrying amount of the asset at the date of change in the estimate.

Assets acquired in exchange for loans

Non-financial assets acquired in exchange for loans as part of an orderly realisation are recorded as assets held for sale and reported in 'Other assets' if the carrying amounts of the assets are recovered principally through sale, the assets are available for sale in their present condition and their sale is highly probable. The asset acquired is recorded at the lower of its fair value less costs to sell and the carrying amount of the loan (net of impairment allowance) at the date of exchange. No depreciation is charged in respect of assets held for sale. Any subsequent write-down of the acquired asset to fair value less costs to sell is recognised in the income statement, in 'Other operating income'. Any subsequent increase in the fair value less costs to sell, to the extent this does not exceed the cumulative write-down, is also recognised in 'Other operating income', together with any realised gains or losses on disposal.

Renegotiated loans

Loans subject to collective impairment assessment whose terms have been renegotiated are no longer considered past due, but are treated as up to date loans for measurement purposes once the minimum number of payments required under the new arrangements have been received. These renegotiated loans are segregated from other parts of the loan portfolio for the purposes of collective impairment assessment, to reflect their risk profile. Loans subject to individual impairment assessment, whose terms have been renegotiated, are subject to ongoing review to determine whether they remain impaired or should be considered past due. The carrying amount of loans that have been classified as renegotiated retain this classification until maturity or derecognition. Interest is recorded on renegotiated loans taking into account the new contractual terms following renegotiation.

(h) Trading assets and trading liabilities

Treasury bills, debt securities, equity securities, loans, deposits, debt securities in issue, and short positions in securities are classified as held for trading if they have been acquired or incurred principally for the purpose of selling or repurchasing in the near term, or they form part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent pattern of short-term profit-taking. These financial assets or financial liabilities are recognised on trade date, when HSBC enters into contractual arrangements with counterparties to purchase or sell the financial instruments, and are normally derecognised when either sold (assets) or extinguished (liabilities). Measurement is initially at fair value, with transaction costs taken to the income statement. Subsequently, the fair values are remeasured, and gains and losses from changes therein are recognised in the income statement in 'Net trading income'.

(i) Financial instruments designated at fair value

Financial instruments, other than those held for trading, are classified in this category if they meet one or more of the criteria set out below, and are so designated by management. HSBC may designate financial instruments at fair value when the designation:

- eliminates or significantly reduces measurement or recognition inconsistencies that would otherwise arise from measuring financial assets or financial liabilities, or recognising gains and losses on them, on different bases. Under this criterion, the main classes of financial instruments designated by HSBC are:

  Long-term debt issues. The interest payable on certain fixed rate long-term debt securities issued has been matched with the interest on 'receive fixed/pay variable' interest rate swaps as part of a documented interest rate risk management strategy. An accounting mismatch would arise if the debt securities issued were accounted for at amortised cost, because the related derivatives are measured at fair value with changes in the fair value recognised in the income statement. By designating the long-term debt at fair value, the movement in the fair value of the long-term debt will also be recognised in the income statement.

  Financial assets and financial liabilities under investment contracts. Liabilities to customers under linked contracts are determined based on the fair value of the assets held in the linked funds, with changes recognised in the income statement. If no designation was made for the assets relating to the customer liabilities they would be classified as available for sale and the changes in fair value would be recorded in other comprehensive income. These financial instruments are managed on a fair value basis and management information is also prepared on this basis. Designation at fair value of the financial assets and liabilities under investment contracts allows the changes in fair values to be recorded in the income statement and presented in the same line.

- applies to groups of financial assets, financial liabilities or combinations thereof that are managed, and their performance evaluated, on a fair value basis in accordance with a documented risk management or investment strategy, and where information about the groups of financial instruments is reported to management on that basis. Under this criterion, certain financial assets held to meet liabilities under insurance contracts are the main class of financial instrument so designated. HSBC has documented risk management and investment strategies designed to manage such assets at fair value, taking into consideration the relationship of assets to liabilities in a way that mitigates market risks. Reports are provided to management on the fair value of the assets. Fair value measurement is also consistent with the regulatory reporting requirements under the appropriate regulations for these insurance operations.

- relates to financial instruments containing one or more embedded derivatives that significantly modify the cash flows resulting from those financial instruments, including certain debt issues and debt securities held.

The fair value designation, once made, is irrevocable. Designated financial assets and financial liabilities are recognised when HSBC enters into the contractual provisions of the arrangements with counterparties, which is generally on trade date, and are normally derecognised when either sold (assets) or extinguished (liabilities). Measurement is initially at fair value, with transaction costs taken to the income statement. Subsequently, the fair values are remeasured, and gains and losses from changes therein are recognised in the income statement in 'Net income from financial instruments designated at fair value'.

(j) Financial investments

Treasury bills, debt securities and equity securities intended to be held on a continuing basis, other than those designated at fair value, are classified as available for sale or held to maturity. Financial investments are recognised on trade date when HSBC enters into contractual arrangements with counterparties to purchase securities, and are normally derecognised when either the securities are sold or the borrowers repay their obligations.

(i) Available-for-sale financial assets are initially measured at fair value plus direct and incremental transaction costs. They are subsequently remeasured at fair value, and changes therein are recognised in other comprehensive income in 'Available-for-sale investments – fair value gains/(losses)' until the financial assets are either sold or become impaired. When available-for-sale financial assets are sold, cumulative gains or losses previously recognised in other comprehensive income are recognised in the income statement as 'Gains less losses from financial investments'.

Interest income is recognised on available-for-sale debt securities using the effective interest rate, calculated over the asset's expected life. Premiums and/or discounts arising on the purchase of dated investment securities are included in the calculation of their effective interest rates. Dividends are recognised in the income statement when the right to receive payment has been established.

At each balance sheet date an assessment is made of whether there is any objective evidence of impairment in the value of a financial asset. Impairment losses are recognised if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the financial asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

If the available-for-sale financial asset is impaired, the difference between the financial asset's acquisition cost (net of any principal repayments and amortisation) and the current fair value, less any previous impairment loss recognised in the income statement, is removed from other comprehensive income and recognised in the income statement.

Impairment losses for available-for-sale debt securities are recognised within 'Loan impairment charges and other credit risk provisions' in the income statement and impairment losses for available-for-sale equity securities are recognised within 'Gains less losses from financial investments' in the income statement. The impairment methodologies for available-for-sale financial assets are set out in more detail below.

– **Available-for-sale debt securities**. When assessing available-for-sale debt securities for objective evidence of impairment at the reporting date, HSBC considers all available evidence, including observable data or information about events specifically relating to the securities which may result in a shortfall in recovery of future cash flows. These events may include a significant financial difficulty of the issuer, a breach of contract such as a default, bankruptcy or other financial reorganisation, or the disappearance of an active market for the debt security because of financial difficulties relating to the issuer.

  These types of specific event and other factors such as information about the issuers' liquidity, business and financial risk exposures, levels of and trends in default for similar financial assets, national and local economic trends and conditions, and the fair value of collateral and guarantees may be considered individually, or in combination, to determine if there is objective evidence of impairment of a debt security.

  In addition, when assessing available-for-sale asset-backed securities ('ABS's) for objective evidence of impairment, HSBC considers the performance of underlying collateral and the extent and depth of market price declines. Changes in credit ratings are considered but a downgrade of a security's credit rating is not, of itself, evidence of impairment. The primary indicators of potential impairment are considered to be adverse fair value movements and the disappearance of an active market for a security. ABS impairment methodologies are described in more detail in 'Securitisation exposures and other structured products' on page 128.

– **Available-for-sale equity securities**. Objective evidence of impairment for available-for sale equity securities may include specific information about the issuer as detailed above, but may also include information about significant changes in technology, markets, economics or the law that provides evidence that the cost of the equity securities may not be recovered.

  A significant or prolonged decline in the fair value of the asset below its cost is also objective evidence of impairment. In assessing whether it is significant, the decline in fair value is evaluated against the original cost of the asset at initial recognition. In assessing whether it is prolonged, the decline is evaluated against the period in which the fair value of the asset has been below its original cost at initial recognition.

Once an impairment loss has been recognised on an available-for-sale financial asset, the subsequent accounting treatment for changes in the fair value of that asset differs depending on the nature of the available-for-sale financial asset concerned:

– for an available-for-sale debt security, a subsequent decline in the fair value of the instrument is recognised in the income statement when there is further objective evidence of impairment as a result of further decreases in the estimated future cash flows of the financial asset. Where there is no further objective evidence of impairment, the decline in the fair value of the financial asset is recognised in other comprehensive income. If the fair value of a debt security increases in a subsequent period, and the increase can be objectively related to an event occurring after the impairment loss was recognised in the income statement, the impairment loss is reversed through the income statement to the extent of the increase in fair value;

– for an available-for-sale equity security, all subsequent increases in the fair value of the instrument are treated as a revaluation and are recognised in other comprehensive income. Impairment losses recognised on the equity security are not reversed through the income statement. Subsequent decreases in the fair value of the available-for-sale equity security are recognised in the income statement, to the extent that further cumulative impairment losses have been incurred in relation to the acquisition cost of the equity security.

(ii) Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that HSBC positively intends, and is able, to hold to maturity. Held-to-maturity investments are initially recorded at fair value plus any directly attributable transaction costs, and are subsequently measured at amortised cost using the effective interest rate method, less any impairment losses.

(k) Sale and repurchase agreements (including stock lending and borrowing)

When securities are sold subject to a commitment to repurchase them at a predetermined price ('repos'), they remain on the balance sheet and a liability is recorded in respect of the consideration received. Securities purchased under commitments to sell ('reverse repos') are not recognised on the balance sheet and the consideration paid is recorded in 'Loans and advances to banks' or 'Loans and advances to customers' as appropriate. The difference between the sale and repurchase price is treated as interest and recognised over the life of the agreement.

Securities lending and borrowing transactions are generally secured, with collateral taking the form of securities or cash advanced or received. The transfer of securities to counterparties under these agreements is not normally reflected on the balance sheet. Cash collateral advanced or received is recorded as an asset or a liability respectively.

Securities borrowed are not recognised on the balance sheet. If they are sold on to third parties, an obligation to return the securities is recorded as a trading liability and measured at fair value, and any gains or losses are included in 'Net trading income'.

(l) Derivatives and hedge accounting

Derivatives are recognised initially, and are subsequently remeasured, at fair value. Fair values of exchange-traded derivatives are obtained from quoted market prices. Fair values of over-the-counter derivatives are obtained using valuation techniques, including discounted cash flow models and option pricing models.

Derivatives may be embedded in other financial instruments, for example, a convertible bond with an embedded conversion option. Embedded derivatives are treated as separate derivatives when their economic characteristics and risks are not clearly and closely related to those of the host contract; the terms of the embedded derivative would meet the definition of a stand-alone derivative if they were contained in a separate contract; and the combined contract is not held for trading or designated at fair value. These embedded derivatives are measured at fair value with changes therein recognised in the income statement.

Derivatives are classified as assets when their fair value is positive, or as liabilities when their fair value is negative. Derivative assets and liabilities arising from different transactions are only offset if the transactions are with the same counterparty, a legal right of offset exists, and the parties intend to settle the cash flows on a net basis.

The method of recognising fair value gains and losses depends on whether derivatives are held for trading or are designated as hedging instruments, and if the latter, the nature of the risks being hedged. All gains and losses from changes in the fair value of derivatives held for trading are recognised in the income statement. When derivatives are designated as hedges, HSBC classifies them as either: (i) hedges of the change in fair value of recognised assets or liabilities or firm commitments ('fair value hedges'); (ii) hedges of the variability in highly probable future cash flows attributable to a recognised asset or liability, or a forecast transaction ('cash flow hedges'); or (iii) a hedge of a net investment in a foreign operation ('net investment hedges'). Hedge accounting is applied to derivatives designated as hedging instruments in a fair value, cash flow or net investment hedge provided certain criteria are met.

Hedge accounting

At the inception of a hedging relationship, HSBC documents the relationship between the hedging instruments and the hedged items, its risk management objective and its strategy for undertaking the hedge. HSBC also requires a documented assessment, both at hedge inception and on an ongoing basis, of whether or not the hedging instruments, primarily derivatives, that are used in hedging transactions are highly effective in offsetting the changes attributable to the hedged risks in the fair values or cash flows of the hedged items. Interest on designated qualifying hedges is included in 'Net interest income'.

Fair value hedge

Changes in the fair value of derivatives that are designated and qualify as fair value hedging instruments are recorded in the income statement, along with changes in the fair value of the hedged assets, liabilities or group thereof that are attributable to the hedged risk.

If a hedging relationship no longer meets the criteria for hedge accounting, the cumulative adjustment to the carrying amount of the hedged item is amortised to the income statement based on a recalculated effective interest rate over the residual period to maturity, unless the hedged item has been derecognised, in which case, it is released to the income statement immediately.

Cash flow hedge

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in other comprehensive income within 'Cash flow hedges – fair value gains/(losses)'. Any gain or loss in fair value relating to an ineffective portion is recognised immediately in the income statement.

The accumulated gains and losses recognised in other comprehensive income are reclassified to the income statement in the periods in which the hedged item will affect profit or loss. However, when the forecast transaction that is hedged results in the recognition of a non-financial asset or a non-financial liability, the gains and losses previously recognised in other comprehensive income are removed from equity and included in the initial measurement of the cost of the asset or liability.

When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss recognised in other comprehensive income at that time remains in equity until the forecast transaction is eventually recognised in the income statement. When a forecast transaction is no longer expected to occur, the cumulative gain or loss that was recognised in other comprehensive income is immediately reclassified to the income statement.

Net investment hedge

Hedges of net investments in foreign operations are accounted for in a similar way to cash flow hedges. A gain or loss on the effective portion of the hedging instrument is recognised in other comprehensive income; a gain or loss on the ineffective portion is recognised immediately in the income statement. Gains and losses previously recognised in other comprehensive income are reclassified to the income statement on the disposal of the foreign operation.

Hedge effectiveness testing

To qualify for hedge accounting, HSBC requires that at the inception of the hedge and throughout its life, each hedge must be expected to be highly effective (prospective effectiveness), and demonstrate actual effectiveness (retrospective effectiveness) on an ongoing basis.

The documentation of each hedging relationship sets out how the effectiveness of the hedge is assessed. The method adopted by an entity to assess hedge effectiveness will depend on its risk management strategy.

For prospective effectiveness, the hedging instrument must be expected to be highly effective in offsetting changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated. For actual effectiveness to be achieved, the changes in fair value or cash flows must offset each other in the range of 80% to 125%.

Hedge ineffectiveness is recognised in the income statement in 'Net trading income'.

Derivatives that do not qualify for hedge accounting

All gains and losses from changes in the fair values of derivatives that do not qualify for hedge accounting are recognised immediately in the income statement. These gains and losses are reported in 'Net trading income', except where derivatives are managed in conjunction with financial instruments designated at fair value (other than derivatives managed in conjunction with debt securities issued by the Group), in which case gains and losses are reported in 'Net income from financial instruments designated at fair value'. The interest on derivatives managed in conjunction with debt securities issued by the Group which are designated at fair value is recognised in 'Interest expense'. All other gains and losses on these derivatives are reported in 'Net income from financial instruments designated at fair value'.

(m) Derecognition of financial assets and liabilities

Financial assets are derecognised when the contractual right to receive cash flows from the assets has expired; or when HSBC has transferred its contractual right to receive the cash flows of the financial assets, and either:

- substantially all the risks and rewards of ownership have been transferred; or
- HSBC has neither retained nor transferred substantially all the risks and rewards, but has not retained control.

Financial liabilities are derecognised when they are extinguished, that is when the obligation is discharged, cancelled, or expires.

(n) Offsetting financial assets and financial liabilities

Financial assets and financial liabilities are offset and the net amount is reported in the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis, or realise the asset and settle the liability simultaneously.

(o) Subsidiaries, associates and joint ventures

HSBC classifies investments in entities which it controls as subsidiaries. Where HSBC is a party to a contractual arrangement whereby, together with one or more parties, it undertakes an economic activity that is subject to joint control, HSBC classifies its interest in the venture as a joint venture. HSBC classifies investments in entities over which it has significant influence, and that are neither subsidiaries nor joint ventures, as associates. For the purpose of determining this classification, control is considered to be the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities.

HSBC Holdings' investments in subsidiaries are stated at cost less any impairment losses. An impairment loss recognised in prior periods shall be reversed through the income statement if, and only if, there has been a change in the estimates used to determine the recoverable amount of the investment in subsidiary since the last impairment loss was recognised.

Investments in associates and interests in joint ventures are recognised using the equity method. Under this method, such investments are initially stated at cost, including attributable goodwill, and are adjusted thereafter for the post-acquisition change in HSBC's share of net assets.

Profits on transactions between HSBC and its associates and joint ventures are eliminated to the extent of HSBC's interest in the respective associates or joint ventures. Losses are also eliminated to the extent of HSBC's interest in the associates or joint ventures unless the transaction provides evidence of an impairment of the asset transferred.

(p) Goodwill and intangible assets

(i) Goodwill arises on the acquisition of subsidiaries, when the aggregate of the fair value of the consideration transferred, the amount of any non-controlling interest and the fair value of any previously held equity interest in the acquiree exceed the amounts of the identifiable assets and liabilities acquired. If they do not exceed the amounts of the identifiable assets and liabilities of an acquired business, the difference is recognised immediately in the income statement. Goodwill arises on the acquisition of interests in joint ventures and associates when the cost of investment exceeds HSBC's share of the net fair value of the associate's or joint venture's identifiable assets and liabilities.

Intangible assets are recognised separately from goodwill when they are separable or arise from contractual or other legal rights, and their fair value can be measured reliably.

Goodwill is allocated to cash-generating units for the purpose of impairment testing, which is undertaken at the lowest level at which goodwill is monitored for internal management purposes. Impairment testing is performed at least annually, and whenever there is an indication that the cash-generating unit may be impaired, by comparing the recoverable amount from a cash-generating unit with the carrying amount of its net assets, including attributable goodwill. The recoverable amount of an asset is the higher of its fair value less cost to sell, and its value in use. Value in use is the present value of the expected future cash flows from a cash-generating unit. If the recoverable amount is less than the carrying value, an impairment loss is charged to the income statement. Goodwill is stated at cost less accumulated impairment losses.

Goodwill on acquisitions of interests in joint ventures and associates is included in 'Interests in associates and joint ventures' and is not tested separately for impairment.

At the date of disposal of a business, attributable goodwill is included in HSBC's share of net assets in the calculation of the gain or loss on disposal.

(ii) Intangible assets include the present value of in-force long-term insurance business, computer software, trade names, mortgage servicing rights, customer lists, core deposit relationships, credit card customer relationships and merchant or other loan relationships. Computer software includes both purchased and internally generated software. The cost of internally generated software comprises all directly attributable costs necessary to create, produce and prepare the software to be capable of operating in the manner intended by management. Costs incurred in the ongoing maintenance of software are expensed immediately as incurred.

Intangible assets are subject to impairment review if there are events or changes in circumstances that indicate that the carrying amount may not be recoverable. Where:

– intangible assets have an indefinite useful life, or are not yet ready for use, they are tested for impairment annually. This impairment test may be performed at any time during the year, provided it is performed at the same time every year. An intangible asset recognised during the current period is tested before the end of the current year; and

– intangible assets have a finite useful life, except for the present value of in-force long-term insurance business, they are stated at cost less amortisation and accumulated impairment losses and are amortised over their estimated useful lives. Estimated useful life is the lower of legal duration and expected useful life. The amortisation of mortgage servicing rights is included within 'Net fee income'.

For the accounting policy governing the present value of in-force long-term insurance business (see Note 2y).

(iii) Intangible assets with finite useful lives are amortised, generally on a straight-line basis, over their useful lives as follows:

Trade names	10 years
Mortgage servicing rights	generally between 5 and 12 years
Internally generated software	between 3 and 5 years
Purchased software	between 3 and 5 years
Customer/merchant relationships	between 3 and 10 years
Other	generally 10 years

(q) Property, plant and equipment

Land and buildings are stated at historical cost, or fair value at the date of transition to IFRSs ('deemed cost'), less any impairment losses and depreciation calculated to write-off the assets over their estimated useful lives as follows:

- freehold land is not depreciated;
- freehold buildings are depreciated at the greater of 2% per annum on a straight-line basis or over their remaining useful lives; and
- leasehold buildings are depreciated over the shorter of their unexpired terms of the leases or their remaining useful lives.

Equipment, fixtures and fittings (including equipment on operating leases where HSBC is the lessor) are stated at cost less any impairment losses and depreciation calculated on a straight-line basis to write-off the assets over their useful lives, which run to a maximum of 35 years but are generally between 5 years and 20 years.

Property, plant and equipment is subject to an impairment review if there are events or changes in circumstances which indicate that the carrying amount may not be recoverable.

HSBC holds certain properties as investments to earn rentals or for capital appreciation, or both. Investment properties are included in the balance sheet at fair value with changes therein recognised in the income statement in the period of change. Fair values are determined by independent professional valuers who apply recognised valuation techniques.

(r) Finance and operating leases

Agreements which transfer to counterparties substantially all the risks and rewards incidental to the ownership of assets, but not necessarily legal title, are classified as finance leases. When HSBC is a lessor under finance leases the amounts due under the leases, after deduction of unearned charges, are included in 'Loans and advances to banks' or 'Loans and advances to customers', as appropriate. The finance income receivable is recognised in 'Net interest income' over the periods of the leases so as to give a constant rate of return on the net investment in the leases.

When HSBC is a lessee under finance leases, the leased assets are capitalised and included in 'Property, plant and equipment' and the corresponding liability to the lessor is included in 'Other liabilities'. A finance lease and its corresponding liability are recognised initially at the fair value of the asset or, if lower, the present value of the minimum lease payments. Finance charges payable are recognised in 'Net interest income' over the period of the lease based on the interest rate implicit in the lease so as to give a constant rate of interest on the remaining balance of the liability.

All other leases are classified as operating leases. When acting as lessor, HSBC includes the assets subject to operating leases in 'Property, plant and equipment' and accounts for them accordingly. Impairment losses are recognised to the extent that residual values are not fully recoverable and the carrying value of the assets is thereby impaired. When HSBC is the lessee, leased assets are not recognised on the balance sheet. Rentals payable and receivable under operating leases are accounted for on a straight-line basis over the periods of the leases and are included in 'General and administrative expenses' and 'Other operating income', respectively.

(s) Income tax

Income tax comprises current tax and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised in other comprehensive income or directly in equity, in which case it is recognised in the same statement in which the related item appears.

Current tax is the tax expected to be payable on the taxable profit for the year, calculated using tax rates enacted or substantively enacted by the balance sheet date, and any adjustment to tax payable in respect of previous years. Current tax assets and liabilities are offset when HSBC intends to settle on a net basis and the legal right to offset exists.

Deferred tax is recognised on temporary differences between the carrying amounts of assets and liabilities in the balance sheet and the amounts attributed to such assets and liabilities for tax purposes. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised.

Deferred tax is calculated using the tax rates expected to apply in the periods in which the assets will be realised or the liabilities settled, based on tax rates and laws enacted, or substantively enacted, by the balance sheet date. Deferred tax assets and liabilities are offset when they arise in the same tax reporting group and relate to income taxes levied by the same taxation authority, and when HSBC has a legal right to offset.

Deferred tax relating to actuarial gains and losses on post-employment benefits is recognised in other comprehensive income. Deferred tax relating to share-based payment transactions is recognised directly in equity to the extent that the amount of the estimated future tax deduction exceeds the amount of the related cumulative remuneration expense. Deferred tax relating to fair value re-measurements of available-for-sale investments and cash flow hedging instruments which are charged or credited directly to other comprehensive income, is also charged or credited to other comprehensive income and is subsequently recognised in the income statement when the deferred fair value gain or loss is recognised in the income statement.

(t) Pension and other post-employment benefits

HSBC operates a number of pension and other post-employment benefit plans throughout the world. These plans include both defined benefit and defined contribution plans and various other post-employment benefits such as post-employment healthcare.

Payments to defined contribution plans and state-managed retirement benefit plans, where HSBC's obligations under the plans are equivalent to a defined contribution plan, are charged as an expense as they fall due.

The defined benefit pension costs and the present value of defined benefit obligations are calculated at the reporting date by the schemes' actuaries using the Projected Unit Credit Method. The net charge to the income statement mainly comprises the current service cost, plus the unwinding of the discount rate on plan liabilities, less the expected return on plan assets, and is presented in operating expenses. Past service costs are charged immediately to the income statement to the extent that the benefits have vested, and are otherwise recognised on a straight-line basis over the average period until the benefits vest. Actuarial gains and losses comprise experience adjustments (the effects of differences between the previous actuarial assumptions and what has actually occurred), as well as the effects of changes in actuarial assumptions. Actuarial gains and losses are recognised in other comprehensive income in the period in which they arise.

The defined benefit liability recognised in the balance sheet represents the present value of defined benefit obligations adjusted for unrecognised past service costs and reduced by the fair value of plan assets. Any net defined benefit surplus is limited to unrecognised past service costs plus the present value of available refunds and reductions in future contributions to the plan.

The cost of obligations arising from other post-employment defined benefit plans, such as defined benefit health-care plans, are accounted for on the same basis as defined benefit pension plans.

(u) Share-based payments

The cost of share-based payment arrangements with employees is measured by reference to the fair value of equity instruments on the date they are granted and recognised as an expense on a straight-line basis over the vesting period, with a corresponding credit to the 'Share-based payment reserve'. The vesting period is the period during which all the specified vesting conditions of a share-based payment arrangement are to be satisfied. The fair value of equity instruments that are made available immediately, with no vesting period attached to the award, are expensed immediately.

Fair value is determined by using appropriate valuation models, taking into account the terms and conditions upon which the equity instruments were granted. Vesting conditions include service conditions and performance conditions; any other features of a share-based payment arrangement are non-vesting conditions. Market performance conditions and non-vesting conditions are taken into account when estimating the fair value of equity instruments at the date of grant, so that an award is treated as vesting irrespective of whether the market performance condition or non-vesting condition is satisfied, provided all other vesting conditions are satisfied.

Vesting conditions, other than market performance conditions, are not taken into account in the initial estimate of the fair value at the grant date. They are taken into account by adjusting the number of equity instruments included in the measurement of the transaction, so that the amount recognised for services received as consideration for the equity instruments granted shall be based on the number of equity instruments that eventually vest. On a cumulative basis, no expense is recognised for equity instruments that do not vest because of a failure to satisfy non-market performance or service conditions.

Where an award has been modified, as a minimum, the expense of the original award continues to be recognised as if it had not been modified. Where the effect of a modification is to increase the fair value of an award or increase the number of equity instruments, the incremental fair value of the award or incremental fair value of the extra equity instruments is recognised in addition to the expense of the original grant, measured at the date of modification, over the modified vesting period.

A cancellation that occurs during the vesting period is treated as an acceleration of vesting, and recognised immediately for the amount that would otherwise have been recognised for services over the vesting period.

Where HSBC Holdings enters into share-based payment arrangements involving employees of subsidiaries, the cost is recognised in 'Investment in subsidiaries' and credited to the 'Share-based payment reserve' over the vesting period. Where a subsidiary funds the share-based payment arrangement, 'Investment in subsidiaries' is reduced by the fair value of equity instruments.

(v) Foreign currencies

Items included in the financial statements of each of HSBC's entities are measured using the currency of the primary economic environment in which the entity operates ('the functional currency'). HSBC's consolidated financial statements are presented in US dollars which is also HSBC Holdings' functional currency.

Transactions in foreign currencies are recorded in the functional currency at the rate of exchange prevailing on the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into the functional currency at the rate of exchange ruling at the balance sheet date. Any resulting exchange differences are included in the income statement. Non-monetary assets and liabilities that are measured at historical cost in a foreign currency are translated into the functional currency using the rate of exchange at the date of the initial transaction. Non-monetary assets and liabilities measured at fair value in a foreign currency are translated into the functional currency using the rate of exchange at the date the fair value was determined. Any exchange component of a gain or loss on a non-monetary item is recognised in other comprehensive income if the gain or loss on the non-monetary item is recognised in other comprehensive income. Any exchange component of a gain or loss on a non-monetary item is recognised in the income statement if the gain or loss on the non-monetary item is recognised in the income statement.

In the consolidated financial statements, the assets, including related goodwill where applicable, and liabilities of branches, subsidiaries, joint ventures and associates whose functional currency is not US dollars, are translated into the Group's presentation currency at the rate of exchange ruling at the balance sheet date. The results of branches, subsidiaries, joint ventures and associates whose functional currency is not US dollars are translated into US dollars at the average rates of exchange for the reporting period. Exchange differences arising from the retranslation of opening foreign currency net assets, and exchange differences arising from retranslation of the result for the reporting period from the average rate to the exchange rate prevailing at the period end, are recognised in other comprehensive income. Exchange differences on a monetary item that is part of a net investment in a foreign operation are recognised in the income statement of the separate financial statements. In consolidated financial statements these exchange differences are recognised in other comprehensive income. On disposal of a foreign operation, exchange differences relating thereto and previously recognised in other comprehensive income are recognised in the income statement.

(w) Provisions

Provisions are recognised when it is probable that an outflow of economic benefits will be required to settle a current legal or constructive obligation, which has arisen as a result of past events, and for which a reliable estimate can be made of the amount of the obligation.

Contingent liabilities, which include certain guarantees and letters of credit pledged as collateral security, are possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence, of one or more uncertain future events not wholly within the control of HSBC; or are present obligations that have arisen from past events but are not recognised because it is not probable that settlement will require the outflow of economic benefits, or because the amount of the obligations cannot be reliably measured. Contingent liabilities are not recognised in the financial statements but are disclosed unless the probability of settlement is remote.

(x) Financial guarantee contracts

Liabilities under financial guarantee contracts which are not classified as insurance contracts are recorded initially at their fair value, which is generally the fee received or receivable. Subsequently, financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure required to settle the obligations.

HSBC Holdings has issued financial guarantees and similar contracts to other Group entities. Where it has previously asserted explicitly that it regards such contracts as insurance contracts and has used accounting applicable to insurance contracts, HSBC may elect to account for guarantees as an insurance contract. This election is made on a contract by contract basis, but the election for each contract is irrevocable. Where these guarantees have been classified as insurance contracts, they are measured and recognised as insurance liabilities.

(y) Insurance contracts

Through its insurance subsidiaries, HSBC issues contracts to customers that contain insurance risk, financial risk or a combination thereof. A contract under which HSBC accepts significant insurance risk from another party by agreeing to compensate that party on the occurrence of a specified uncertain future event, is classified as an insurance contract. An insurance contract may also transfer financial risk, but is accounted for as an insurance contract if the insurance risk is significant.

While investment contracts with discretionary participation features are financial instruments, they continue to be treated as insurance contracts as permitted by IFRS 4.

Insurance contracts are accounted for as follows:

Premiums

Gross insurance premiums for non-life insurance business are reported as income over the term of the insurance contracts based on the proportion of risks borne during the accounting period. The unearned premium (the proportion of the business underwritten in the accounting year relating to the period of risk after the balance sheet date) is calculated on a daily or monthly pro rata basis.

Premiums for life insurance contracts are accounted for when receivable, except in unit-linked insurance contracts where premiums are accounted for when liabilities are established.

Reinsurance premiums are accounted for in the same accounting period as the premiums for the direct insurance contracts to which they relate.

Claims and reinsurance recoveries

Gross insurance claims for non-life insurance contracts include paid claims and movements in outstanding claims liabilities.

Gross insurance claims for life insurance contracts reflect the total cost of claims arising during the year, including claim handling costs and any policyholder bonuses allocated in anticipation of a bonus declaration. Claims arising during the year include maturities, surrenders and death claims.

Maturity claims are recognised when due for payment. Surrenders are recognised when paid or at an earlier date on which, following notification, the policy ceases to be included within the calculation of the related insurance liabilities. Death claims are recognised when notified.

Reinsurance recoveries are accounted for in the same period as the related claim.

Liabilities under insurance contracts

Outstanding claims liabilities for non-life insurance contracts are based on the estimated ultimate cost of all claims incurred but not settled at the balance sheet date, whether reported or not, together with related claim-handling costs and a reduction for the expected value of salvage and other recoveries. Liabilities for claims incurred but not reported are made on an estimated basis, using appropriate statistical techniques.

Liabilities under non-linked life insurance contracts are calculated by each life insurance operation based on local actuarial principles.

Liabilities under unit-linked life insurance contracts are at least equivalent to the surrender or transfer value which is calculated by reference to the value of the relevant underlying funds or indices.

A liability adequacy test is carried out on insurance liabilities to ensure that the carrying amount of the liabilities is sufficient in the light of current estimates of future cash flows. When performing the liability adequacy test, all contractual cash flows are discounted and compared with the carrying value of the liability. When a shortfall is identified it is charged immediately to the income statement.

Present value of in-force long-term insurance business

The value placed on insurance contracts that are classified as long-term insurance business or long-term investment contracts with discretionary participating features ('DPF') and are in force at the balance sheet date is recognised as an asset. The asset represents the present value of the equity holders' interest in the profits expected to emerge from these contracts written at the balance sheet date.

The present value of in-force long-term insurance business and long-term investment contracts with DPF, referred to as 'PVIF', is determined by discounting the equity holders' interest in future profits expected to emerge from business currently in force using appropriate assumptions in assessing factors such as future mortality, lapse rates and levels of expenses and a risk discount rate that reflects the risk premium attributable to the respective contracts. The PVIF incorporates allowances for both non-market risk and the value of financial options and guarantees. The PVIF asset is presented gross of attributable tax in the balance sheet and movements in the PVIF asset are included in 'Other operating income' on a gross of tax basis.

Future profit participation

Where contracts provide discretionary profit participation benefits to policyholders, liabilities for these contracts include provisions for the future discretionary benefits to policyholders. These provisions reflect actual performance of the investment portfolio to date and management expectation on the future performance in connection with the assets backing the contracts, as well as other experience factors such as mortality, lapses and operational efficiency, where appropriate. This benefit may arise from the contractual terms, regulation, or past distribution policy.

In the case of net unrealised investment gains on contracts whose discretionary benefits principally reflect the actual performance of the investment portfolio, the corresponding increase in the liabilities is recognised in either the income statement or other comprehensive income, following the treatment of the unrealised gains on the relevant assets. In the case of net unrealised losses, a deferred participating asset is recognised only to the extent that its recoverability is highly probable. Movements in the liabilities arising from realised gains and losses on relevant assets are recognised in the income statement.

Investment contracts

Customer liabilities under linked and certain non-linked investment contracts and the corresponding financial assets are designated at fair value. Movements in fair value are recognised in 'Net income from financial investments designated at fair value'. Premiums receivable and amounts withdrawn are accounted for as increases or decreases in the liability recorded in respect of investment contracts.

Liabilities under linked investment contracts are at least equivalent to the surrender or transfer value which is calculated by reference to the value of the relevant underlying funds or indices.

Investment management fees receivable are recognised in the income statement over the period of the provision of the investment management services, in 'Net fee income'.

The incremental costs directly related to the acquisition of new investment contracts or renewing existing investment contracts are deferred and amortised over the period during which the investment management services are provided.

(z) Debt securities issued and deposits by customers and banks

Financial liabilities are recognised when HSBC enters into the contractual provisions of the arrangements with counterparties, which is generally on trade date, and initially measured at fair value, which is normally the consideration received, net of directly attributable transaction costs incurred. Subsequent measurement of financial liabilities, other than those measured at fair value through profit or loss and financial guarantees, is at amortised cost, using the effective interest method to amortise the difference between proceeds received, net of directly attributable transaction costs incurred, and the redemption amount over the expected life of the instrument.

(aa) Share capital

Shares are classified as equity when there is no contractual obligation to transfer cash or other financial assets. Incremental costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax.

HSBC Holdings plc shares held by HSBC are recognised in equity as a deduction from retained earnings until they are cancelled. When such shares are subsequently sold, reissued or otherwise disposed of, any consideration received is included in equity, net of any directly attributable incremental transaction costs and related income tax effects.

(ab) Cash and cash equivalents

For the purpose of the statement of cash flows, cash and cash equivalents include highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of change in value. Such investments are normally those with less than three months' maturity from the date of acquisition, and include cash and balances at central banks, treasury bills and other eligible bills, loans and advances to banks, items in the course of collection from or in transmission to other banks, and certificates of deposit.

(ac) Rights issues

Rights issues to acquire a fixed number of the entity's own equity instruments for a fixed amount of any currency are equity instruments if the entity offers the rights issues pro rata to all of its existing owners of the same class of its own non-derivative equity instruments. On initial recognition, these rights are recognised in shareholders' equity and are not subsequently re-measured during the offer period. Following the exercise of the rights and the allotment of new shares, the cash proceeds of the rights issue are recognised in shareholders' equity. Incremental costs directly attributable to the rights issue are shown as a deduction from the proceeds, net of tax.

3 Net income/(expense) from financial instruments designated at fair value

Net income/(expense) from financial instruments designated at fair value includes:

- all gains and losses from changes in the fair value of financial assets and liabilities designated at fair value, including liabilities under investment contracts;
- all gains and losses from changes in the fair value of derivatives that are managed in conjunction with financial assets and liabilities designated at fair value; and
- interest income, interest expense and dividend income in respect of:
  - financial assets and liabilities designated at fair value; and
  - derivatives managed in conjunction with the above,

  except for interest arising from HSBC's issued debt securities and derivatives managed in conjunction with those debt securities, which is recognised in 'Interest expense'.

Net income/(expense) from financial instruments designated at fair value

HSBC

	2010 US$m	2009 US$m	2008 US$m
Net income/(expense) arising on:			
– financial assets held to meet liabilities under insurance and investment contracts	**2,349**	3,793	(5,064)
– other financial assets designated at fair value	**230**	2	1,738
– derivatives managed in conjunction with other financial assets designated at fair value	**(149)**	(249)	77
	2,430	3,546	(3,249)
– liabilities to customers under investment contracts	**(946)**	(1,329)	1,751
– HSBC's long-term debt issued and related derivatives	**(258)**	(6,247)	6,679
– changes in own credit spread on long-term debt	**(63)**	(6,533)	6,570
– derivatives managed in conjunction with HSBC's issued debt securities	**(275)**	(1,726)	4,413
– other changes in fair value	**80**	2,012	(4,304)
– other financial liabilities designated at fair value	**(18)**	492	(1,368)
– derivatives managed in conjunction with other financial liabilities designated at fair value	**12**	7	39
	(1,210)	(7,077)	7,101
	1,220	(3,531)	3,852

HSBC Holdings

	2010 US$m	2009 US$m	2008 US$m
Net income/(expense) arising on HSBC Holdings long-term debt issued and related derivatives			
– changes in own credit spread on long-term debt	**248**	(2,612)	2,262
– derivatives managed in conjunction with HSBC Holdings issued debt securities	**(482)**	(352)	688
– other changes in fair value	**373**	201	37
	139	(2,763)	2,987

Notes on the Financial Statements (continued)

4 Net earned insurance premiums

	Non-life insurance US$m	Life insurance (non-linked) US$m	Life insurance (linked) US$m	Investment contracts with DPF[1] US$m	Total US$m
2010					
Gross earned premiums	**1,275**	**5,427**	**1,956**	**2,951**	**11,609**
– gross written premiums	**1,192**	**5,357**	**1,956**	**2,951**	**11,456**
– movement in unearned premiums	**83**	**70**	**–**	**–**	**153**
Reinsurers' share of gross earned premiums	**(160)**	**(289)**	**(14)**	**–**	**(463)**
– gross written premiums ceded to reinsurers	**(172)**	**(266)**	**(8)**	**–**	**(446)**
– reinsurers' share of movement in unearned premiums	**12**	**(23)**	**(6)**	**–**	**(17)**
	1,115	**5,138**	**1,942**	**2,951**	**11,146**
2009					
Gross earned premiums	1,572	5,218	1,427	2,774	10,991
– gross written premiums	1,339	5,285	1,427	2,774	10,825
– movement in unearned premiums	233	(67)	–	–	166
Reinsurers' share of gross earned premiums	(225)	(278)	(17)	–	(520)
– gross written premiums ceded to reinsurers	(215)	(280)	(11)	–	(506)
– reinsurers' share of movement in unearned premiums	(10)	2	(6)	–	(14)
	1,347	4,940	1,410	2,774	10,471
2008					
Gross earned premiums	1,834	6,086	1,825	2,802	12,547
– gross written premiums	1,776	6,257	1,825	2,802	12,660
– movement in unearned premiums	58	(171)	–	–	(113)
Reinsurers' share of gross earned premiums	(263)	(851)	(583)	–	(1,697)
– gross written premiums ceded to reinsurers	(260)	(878)	(564)	–	(1,702)
– reinsurers' share of movement in unearned premiums	(3)	27	(19)	–	5
	1,571	5,235	1,242	2,802	10,850

1 *Discretionary participation features.*

5 Net insurance claims incurred and movement in liabilities to policyholders

	Non-life insurance US$m	Life insurance (non-linked) US$m	Life insurance (linked) US$m	Investment contracts with DPF[1] US$m	Total US$m
2010					
Gross claims incurred and movement in liabilities	**625**	**5,108**	**2,520**	**3,716**	**11,969**
– claims, benefits and surrenders paid	**815**	**1,355**	**507**	**2,023**	**4,700**
– movement in liabilities	**(190)**	**3,753**	**2,013**	**1,693**	**7,269**
Reinsurers' share of claims incurred and movement in liabilities	**(100)**	**(201)**	**99**	**–**	**(202)**
– claims, benefits and surrenders paid	**(114)**	**(143)**	**(45)**	**–**	**(302)**
– movement in liabilities	**14**	**(58)**	**144**	**–**	**100**
	525	**4,907**	**2,619**	**3,716**	**11,767**

	Non-life insurance US$m	Life insurance (non-linked) US$m	Life insurance (linked) US$m	Investment contracts with DPF[1] US$m	Total US$m
2009					
Gross claims incurred and movement in liabilities	1,281	4,669	2,676	3,934	12,560
– claims, benefits and surrenders paid	987	2,098	325	1,818	5,228
– movement in liabilities	294	2,571	2,351	2,116	7,332
Reinsurers' share of claims incurred and movement in liabilities	(158)	(98)	146	–	(110)
– claims, benefits and surrenders paid	(156)	(159)	(21)	–	(336)
– movement in liabilities	(2)	61	167	–	226
	1,123	4,571	2,822	3,934	12,450
2008					
Gross claims incurred and movement in liabilities	1,044	5,480	939	1,743	9,206
– claims, benefits and surrenders paid	1,044	1,491	481	1,911	4,927
– movement in liabilities	–	3,989	458	(168)	4,279
Reinsurers' share of claims incurred and movement in liabilities	(83)	(792)	(1,442)	–	(2,317)
– claims, benefits and surrenders paid	(158)	(172)	(44)	–	(374)
– movement in liabilities	75	(620)	(1,398)	–	(1,943)
	961	4,688	(503)	1,743	6,889

1 *Discretionary participation features.*

6 Net operating income

Net operating income is stated after the following items of income, expense, gains and losses:

	2010 US$m	2009 US$m	2008 US$m
Income			
Interest recognised on impaired financial assets	**516**	941	1,040
Fees earned on financial assets or liabilities not held for trading nor designated at fair value, other than fees included in effective interest rate calculations on these types of assets and liabilities	**11,445**	12,310	14,511
Fees earned on trust and other fiduciary activities where HSBC holds or invests assets on behalf of its customers	**3,074**	2,735	3,314
Income from listed investments	**7,418**	9,201	11,425
Income from unlisted investments	**7,187**	7,085	11,359
Losses from the fraud at Bernard L Madoff Investment Securities LLC (within net trading income)	**–**	(72)	(984)
Gain arising from dilution of interests in associates	**188**	–	–
Expense			
Interest on financial instruments, excluding interest on financial liabilities held for trading or designated at fair value	**(17,549)**	(19,737)	(45,525)
Fees payable on financial assets or liabilities not held for trading nor designated at fair value, other than fees included in effective interest rate calculations on these types of assets and liabilities	**(1,529)**	(1,580)	(1,866)
Fees payable relating to trust and other fiduciary activities where HSBC holds or invests assets on behalf of its customers	**(151)**	(116)	(159)
Gains/(losses)			
Gain on disposal or settlement of loans and advances	**121**	244	94
Impairment of available-for-sale equity securities	**(105)**	(358)	(1,042)
Gains on disposal of property, plant and equipment, intangible assets and non-financial investments	**639**	457	465
Gain on sale/repurchase of properties	**250**	576	416
Loan impairment charges and other credit risk provisions	**(14,039)**	(26,488)	(24,937)
Net impairment charge on loans and advances	**(13,548)**	(24,942)	(24,131)
Impairment of available-for-sale debt securities	**(472)**	(1,474)	(737)
Impairment in respect of other credit risk provisions	**(19)**	(72)	(69)

7 Employee compensation and benefits

	2010 US$m	2009 US$m	2008 US$m
Wages and salaries	**17,193**	16,268	18,169
Social security costs	**1,567**	1,512	1,625
Post-employment benefits	**1,076**	688	998
	19,836	18,468	20,792

Average number of persons employed by HSBC during the year

	2010	2009	2008
Europe	**79,902**	84,056	87,864
Hong Kong	**29,105**	28,894	30,030
Rest of Asia-Pacific	**89,737**	88,122	87,954
Middle East	**8,983**	8,468	8,201
North America	**36,822**	42,202	53,090
Latin America	**57,778**	57,774	64,319
Total	**302,327**	309,516	331,458

Post-employment benefit plans

Income statement charge

	2010 US$m	2009 US$m	2008 US$m
Defined benefit pension plans	**468**	161	477
– HSBC Bank (UK) Pension Scheme	**308**	(179)	255
– Other plans	**160**	340	222
Defined contribution pension plans	**545**	492	498
	1,013	653	975
Defined benefit healthcare plans	**58**	31	13
Defined contribution healthcare plans	**5**	4	10
	1,076	688	998

Net assets/(liabilities) recognised on balance sheet in respect of defined benefit plans

	2010 US$m	2009 US$m
Defined benefit pension plans	**(2,867)**	(6,147)
HSBC Bank (UK) Pension Scheme	**(622)**	(3,822)
– fair value of plan assets	**22,236**	17,701
– present value of defined benefit obligations	**(22,858)**	(21,523)
Other plans	**(2,245)**	(2,325)
– fair value of plan assets	**7,559**	6,822
– present value of defined benefit obligations	**(9,785)**	(9,109)
– effect of limit on plan surpluses	**(47)**	(47)
– unrecognised past service cost	**28**	9
Defined benefit healthcare plans	**(946)**	(820)
– fair value of plan assets	**165**	142
– present value of defined benefit obligations	**(1,087)**	(937)
– unrecognised past service cost	**(24)**	(25)
Fair value of plan assets	**29,960**	24,665
Present value of defined benefit obligations	**(33,730)**	(31,569)
Effect of limit on plan surpluses	**(47)**	(47)
Unrecognised past service cost	**4**	(16)
	(3,813)	(6,967)
Retirement benefit liabilities	**(3,856)**	(6,967)
Retirement benefit assets	**43**	–

Cumulative actuarial gains/(losses) recognised in other comprehensive income

	2010 US$m	2009 US$m
At 1 January	**(4,660)**	(1,074)
HSBC Bank (UK) Pension Scheme	**321**	(3,692)
Other plans	**(275)**	179
Healthcare plans	**(112)**	(36)
Change in the effect of limit on plan surpluses[1]	**6**	(37)
Total actuarial losses recognised in other comprehensive income	**(60)**	(3,586)
At 31 December[2]	**(4,720)**	(4,660)

1 *Excludes exchange differences of US$6m (2009: US$1m).*
2 *Includes cumulative movements related to the limit on plan surpluses. This limit is US$47m at 31 December 2010 (2009: US$47m).*

HSBC pension plans

	2010	2009	2008
Number of plans worldwide	**218**	211	205
	%	%	%
Percentage of HSBC employees:			
– enrolled in defined contribution plans	**63**	59	50
– enrolled in defined benefit plans	**27**	29	36
– covered by HSBC pension plans	**90**	88	86

HSBC has been progressively offering all new employees membership of defined contribution plans.

The majority of the Group's defined benefit plans are funded plans. The assets of most of the larger plans are held in trusts or similar funds separate from HSBC. The plans are reviewed at least annually or in accordance with local practice and regulations by qualified actuaries. The actuarial assumptions used to calculate the defined benefit obligations and related current service costs vary according to the economic conditions of the countries in which the plans are situated.

Pension plans in the UK

The largest plan exists in the UK, where the HSBC Bank (UK) Pension Scheme ('the Scheme') covers employees of HSBC Bank plc and certain other employees of HSBC. This comprises a funded defined benefit plan ('the principal plan'), which is closed to new entrants, and a defined contribution plan which was established in July 1996 for new employees.

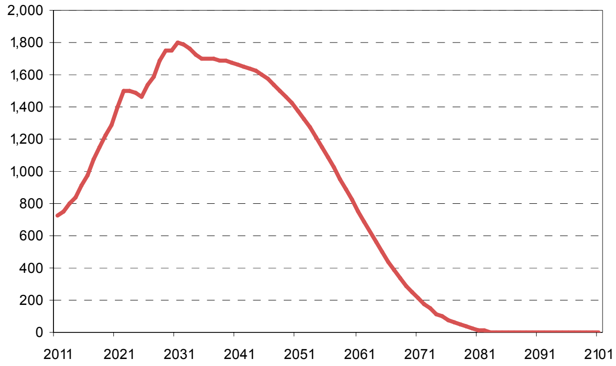
The latest actuarial valuation of the principal plan was made as at 31 December 2008 by C G Singer, Fellow of the Institute of Actuaries, of Towers Watson Limited. At that date, the market value of the HSBC Bank (UK) Pension Scheme's assets was £10.6bn (US$15.5bn) (including assets relating to the defined benefit plan, the defined contribution plan and additional voluntary contributions). The market value of the plan assets represented 77% of the amount expected to be required, on the basis of the assumptions adopted, to provide the benefits accrued to members after allowing for expected future increases in earnings, and the resulting deficit amounted to £3.2bn (US$4.7bn). The method adopted for this investigation was the projected unit method.

The expected cash flows from the principal plan were projected by reference to the Retail Price Index ('RPI') swap break-even curve at 31 December 2008. Salary increases were assumed to be 0.5% per annum above RPI and inflationary pension increases, subject to a minimum of zero per cent and a maximum of 5% (maximum of 3% per annum in respect of service accrued since 1 July 2009), were assumed to be in line with RPI. The projected cash flows were discounted at the LIBOR swap curve at 31 December 2008 plus a margin for the expected return on the investment strategy of 190 basis points per annum. The mortality experience of the principal plan's pensioners over the three year period since the previous valuation was analysed and, on the basis of this analysis, the mortality assumptions were set based on the SAPS S1 series of tables which best fit the pensioner experience. Allowance was made for future improvements to mortality rates in line with the medium cohort projections with a minimum improvement rate set at 1.75% for males and 1.25% for females. The benefits payable from the defined benefit plan are expected to be as shown in the chart below.

Notes on the Financial Statements (continued)

7 – Employee compensation and benefits

Benefit payments (US$m)



The expected cash flows of the principal plan were projected by reference to the RPI swap curve in calculating the liability recognised. The Occupational Pensions (Revaluation) Order 2010 confirmed the UK Government's intention to move to using the Consumer Prices Index ('CPI') rather than RPI as the inflation measure for determining the minimum pension increases to be applied to the statutory index-linked features of retirement benefits. Historical annual CPI increases have generally been lower than annual RPI increases. The rules of the principal plan prescribe that annual increases will be in line with RPI for pensions in payment and statutory index-linked prior to retirement for deferred pensions. In respect of deferred pensioners, consistent with communications to scheme members, HSBC continued to use RPI in calculating the liability recognised as at 31 December 2010. Using CPI to value the schemes liabilities in respect of deferred pensioners would result in a reduction in the principal plan's liabilities of approximately US$400m based on the financial and demographic assumptions as at 31 December 2010.

As part of the 31 December 2008 valuation, calculations were also carried out as to the amount of assets that might be needed to meet the liabilities if the Scheme was discontinued and the members' benefits bought out with an insurance company (although in practice this may not be possible for a plan of this size) or the Trustee continued to run the plan without the support of HSBC. The amount required under this approach is estimated to be £19.8bn (US$28.9bn) as at 31 December 2008. In arriving at this estimation, a more prudent assumption about future mortality was made than for the assessment of the ongoing position and it was assumed that the Trustee would alter the investment strategy to be an appropriately matched portfolio of UK government bonds. An explicit allowance for expenses was also included.

Information on the investment strategy of the principal plan can be found on page 172.

In February 2010, HSBC Bank plc agreed with the Trustee of the Scheme to reduce the deficit of the plan by meeting a schedule of future funding payments. On 17 June 2010, HSBC Bank plc agreed with the Trustee to accelerate the reduction of the deficit of the plan with a special contribution of £1,760m (US$2,638m) in 2010 followed by a revised payment schedule in the following years, as shown below:

Additional future funding payments to the principal plan

	Original plan US$m[1]	Original plan £m	Revised plan US$m[1]	Revised plan £m
2011	–	–	–	–
2012	722	465	–	–
2013	722	465	–	–
2014	722	465	–	–
2015	978	630	–	–
2016	978	630	768	495
2017	978	630	978	630
2018	978	630	978	630

1 *The payment schedule was agreed with the Trustee in pounds sterling and the equivalent US dollar amounts are shown at the exchange rate effective as at 31 December 2010.*

HSBC considers that the contributions set out above, together with investment returns at an expected level of 240 basis points above the LIBOR swap curve, would be sufficient to meet the deficit as at 31 December 2008 over the agreed period. At each subsequent actuarial valuation, HSBC has agreed with the Trustee that any shortfall in investment returns relative to this expected level, subject to a maximum of 50 basis points per annum, will be eliminated by payment of equal cash instalments over the remaining years to the end of this recovery plan period.

HSBC Bank plc also agreed to make ongoing contributions to the principal plan in respect of the accrual of benefits of defined benefit section members at the rate of 34% of pensionable salaries (less member contributions) payable from 1 April 2010 until the completion of the next actuarial valuation, due as at 31 December 2011. During 2009, HSBC paid contributions at the rate of 38% of pensionable salaries (less member contributions) and continued contributions at this rate until 31 March 2010.

On 1 July 2009, changes to the design of the defined benefit section of the principal plan were made. This included the introduction of employee contributions, optionality concerning future benefit accrual and, with effect from 1 April 2010, an increased normal retirement age of 65 years. In addition, enhancements to the defined contribution section were also introduced.

Pension plans in Hong Kong

In Hong Kong, the HSBC Group Hong Kong Local Staff Retirement Benefit Scheme covers employees of The Hongkong and Shanghai Banking Corporation and certain other employees of HSBC. The scheme comprises a funded defined benefit scheme (which provides a lump sum on retirement but is now closed to new members) and a defined contribution scheme. The latter was established on 1 January 1999 for new employees. The latest actuarial valuation of the defined benefit scheme was made at 31 December 2009, and was performed by Estella Chiu, fellow of the Society of Actuaries of the United States of America, of HSBC Insurance (Asia) Limited, a subsidiary of HSBC Holdings. At that valuation date, the market value of the defined benefit scheme's assets was US$1,088m. On an ongoing basis, the actuarial value of the scheme's assets represented 105% of the actuarial present value of the benefits accrued to members, after allowing for expected future increases in salaries, and the resulting surplus amounted to US$71m. On a wind-up basis, the scheme's assets represented 107% of the members' vested benefits, based on current salaries, and the resulting surplus amounted to US$89m. The attained age method has been adopted for the valuation and the major assumptions used in this valuation were a discount rate of 6% per annum and long-term salary increases of 5% per annum.

Pension plans in North America

The HSBC North America (US) Retirement Income Plan covers all employees of HSBC Bank USA, HSBC Finance and other HSBC entities in the US who have reached the age of 21 and met the one year of service participation requirement. The Retirement Income Plan is a funded defined benefit plan which provides final average pay benefits to legacy participants and cash balance benefits to all other participants. All new employees participate in the cash balance section of the plan. In November 2009, the Board of Directors of HSBC North America Holdings, Inc. ('HNAH') approved actions to cease all future benefit accruals for legacy participants under the final average pay formula components of the HSBC North America Retirement Income Plan with effect from 1 January 2011. Affected employees were informed of this decision in February 2010. As a result of these changes, HNAH recorded a one-time curtailment gain of US$144m.

The most recent actuarial valuation of the plan to determine compliance with US statutory funding requirements was made at 1 January 2010 by Jennifer Jakubowski, Fellow of the Society of Actuaries, Enrolled Actuary, member of the American Academy of Actuaries, of Mercer. At that date, the market value of the plan's assets was US$2,321m. The assets represented 85% of the benefits accrued to members as valued under the provisions of the Pension Protection Act of 2006 that was effective for the plan year beginning 1 January 2008. The resulting deficit amounted to US$400m. The method employed for this valuation was the traditional unit credit method and the discount rate was determined using a segment rate method as selected by HSBC under the relevant regulations, which resulted in an effective interest rate of 6.64% per annum.

These determinations described above for actuarial funding valuation purposes are based on different methods and assumptions than those used for financial reporting purposes, and as a result should neither be compared nor related to other determinations included in these financial statements.

The HSBC Bank (UK) Pension Scheme, The HSBC Group Hong Kong Local Staff Retirement Benefit Scheme, and the HSBC North America (US) Retirement Income Plan cover 34% of HSBC's employees and represent 82% of the Group's present value of defined benefit obligations.

Notes on the Financial Statements (continued)

HSBC healthcare benefits plans

HSBC also provides post-employment healthcare benefits under plans in the UK, the US, Bermuda, Canada, Mexico and Brazil, the majority of which are unfunded. The majority of post-employment healthcare benefits plans are defined benefit plans and are accounted for in the same manner as defined benefit pension plans. The plans are reviewed at least annually or in accordance with local practice and regulations by qualified actuaries. The actuarial assumptions used to calculate the defined benefit obligation and related current service cost vary according to the economic conditions of the countries in which they are situated.

Defined benefit pension plans

Net liability under defined benefit pension plans

	HSBC Bank (UK) Pension Scheme		Other plans	
	2010	2009	**2010**	2009
	US$m	US$m	**US$m**	US$m
Fair value of plan assets				
At 1 January	**17,701**	14,865	**6,822**	6,024
Expected return on plan assets	**1,092**	959	**437**	381
Contributions by HSBC	**2,890**	367	**422**	596
– normal	**252**	367	**194**	178
– special	**2,638**	–	**228**	418
Contributions by employees	**23**	5	**17**	17
Experience gains	**1,772**	871	**394**	65
Benefits paid	**(744)**	(884)	**(440)**	(522)
Transfers	**136**	–	**(136)**	–
Assets distributed on curtailments	**–**	–	**(7)**	(5)
Assets distributed on settlements	**–**	–	**(10)**	(6)
Exchange differences	**(634)**	1,518	**60**	272
At 31 December	**22,236**	17,701	**7,559**	6,822
Present value of defined benefit obligations				
At 1 January	**(21,523)**	(15,257)	**(9,109)**	(8,787)
Current service cost	**(252)**	(260)	**(300)**	(334)
Interest cost	**(1,148)**	(1,019)	**(438)**	(397)
Contributions by employees	**(23)**	(5)	**(17)**	(17)
Actuarial (losses)/gains	**(1,451)**	(4,563)	**(669)**	114
Benefits paid	**744**	884	**518**	608
Past service cost – vested immediately	**–**	–	**(11)**	(20)
Past service cost – unvested benefits	**–**	–	**(20)**	–
Business combinations	**–**	–	**–**	(4)
Transfers	**(136)**	–	**136**	–
Reduction in liabilities resulting from curtailments	**–**	–	**158**	41
Liabilities extinguished on settlements	**–**	499	**12**	1
Exchange differences	**931**	(1,802)	**(45)**	(314)
At 31 December	**(22,858)**	(21,523)	**(9,785)**	(9,109)
Funded	**(22,858)**	(21,523)	**(9,241)**	(8,588)
Unfunded	**–**	–	**(544)**	(521)
Effect of limit on plan surpluses	**–**	–	**(47)**	(47)
Unrecognised past service cost	**–**	–	**28**	9
Net liability	**(622)**	(3,822)	**(2,245)**	(2,325)
Retirement benefit liabilities recognised in the balance sheet	**(622)**	(3,822)	**(2,288)**	(2,325)
Retirement benefit assets recognised in the balance sheet (within ‘Other assets’)	**–**	–	**43**	–

Plan assets of the Group’s pension schemes included US$57m (2009: US$62m) of equities and US$1m (2009: US$2m) of bonds issued by HSBC and US$1,592m (2009: US$1,925m) of other assets placed or transacted with HSBC. The fair value of plan assets included derivatives entered into with HSBC Bank plc by the HSBC Bank (UK) Pension Scheme with a positive fair value of US$2,173m at 31 December 2010 (2009: US$1,049m positive fair value) and US$77m positive fair value (2009: US$27m positive fair value) in respect of the HSBC International Staff Retirement Benefits Scheme. Further details of these swap arrangements are included in Note 45.

On 17 June 2010, HSBC Bank plc made a £1,760m (US$2,638m) special contribution to accelerate the reduction of the deficit of the HSBC Bank (UK) Pension Scheme. On the same day the Scheme used the contribution to acquire debt securities with a fair value of £1,760m (US$2,638m) from HSBC in a transaction at an arm's length value determined by the Scheme's independent third-party advisors. The debt securities sold comprised supranational, agency and government-guaranteed securities, asset-backed securities, corporate subordinated debt and auction rate securities. The contribution together with net actuarial gains of US$321m helped achieve a reduction in the net liability of the scheme from US$3,822m at 31 December 2009 to US$622m at 31 December 2010.

The special contributions of US$228m to other plans include an additional contribution of US$187m to the HSBC North America (US) Retirement Income Plan which was made to maintain a minimum funding level.

The actual return on plan assets for the year ended 31 December 2010 was a positive return of US$3,695m (2009: positive US$2,276m).

HSBC expects to make US$880m of contributions to defined benefit pension plans during 2011. Benefits expected to be paid from the plans to retirees over each of the next five years, and in aggregate for the five years thereafter, are as follows:

Benefits expected to be paid from plans

	2011 US$m	2012 US$m	2013 US$m	2014 US$m	2015 US$m	2016-2020 US$m
HSBC Bank (UK) Pension Scheme ..	716	745	790	835	903	5,665
Other significant plans	502	506	528	568	579	3,639

Total (income)/expense recognised in the income statement in 'Employee compensation and benefits'

	HSBC Bank (UK) Pension Scheme			Other plans		
	2010 **US$m**	2009 US$m	2008 US$m	**2010** **US$m**	2009 US$m	2008 US$m
Current service cost	**252**	260	387	**300**	334	357
Interest cost	**1,148**	1,019	1,227	**438**	397	466
Expected return on plan assets	**(1,092)**	(959)	(1,359)	**(437)**	(381)	(549)
Past service cost	**–**	–	–	**12**	21	9
Gains on curtailments	**–**	–	–	**(151)**	(36)	(20)
(Gains)/losses on settlements	**–**	(499)	–	**(2)**	5	(41)
Total (income)/expense	**308**	(179)	255	**160**	340	222

The US$499m settlement gain in 2009 relates to an accounting benefit following a restructuring of the basis of delivery of death in service and ill health early retirement benefits to certain UK employees.

Summary

	HSBC Bank (UK) Pension Scheme				
	2010 **US$m**	2009 US$m	2008 US$m	2007 US$m	2006 US$m
Defined benefit obligation	**(22,858)**	(21,523)	(15,257)	(23,512)	(24,332)
Fair value of plan assets	**22,236**	17,701	14,865	22,704	20,587
Net deficit	**(622)**	(3,822)	(392)	(808)	(3,745)
Experience gains/(losses) on plan liabilities	**(327)**	(234)	(49)	(64)	540
Experience gains/(losses) on plan assets	**1,772**	871	(2,861)	29	–
Gains/(losses) from changes in actuarial assumptions	**(1,124)**	(4,329)	3,081	2,459	(570)
Total net actuarial gains/(losses)	**321**	(3,692)	171	2,424	(30)

Notes on the Financial Statements (continued)

7 – Employee compensation and benefits

Summary (continued)

	Other plans				
	2010 US$m	2009 US$m	2008 US$m	2007 US$m	2006 US$m
Defined benefit obligation	**(9,785)**	(9,109)	(8,787)	(8,873)	(7,916)
Fair value of plan assets	**7,559**	6,822	6,024	7,768	7,116
Net deficit	**(2,226)**	(2,287)	(2,763)	(1,105)	(800)
Experience gains/(losses) on plan liabilities	**(73)**	20	(52)	(354)	(167)
Experience gains/(losses) on plan assets	**394**	65	(1,452)	157	203
Gains/(losses) from changes in actuarial assumptions	**(596)**	94	(306)	(121)	(44)
Total net actuarial gains/(losses)	**(275)**	179	(1,810)	(318)	(8)

Defined benefit healthcare plans

Net liability under defined benefit healthcare plans

	2010 US$m	2009 US$m
Fair value of plan assets		
At 1 January	**142**	128
Expected return on plan assets	**13**	11
Contributions by HSBC	**9**	11
Experience gains	**6**	8
Benefits paid	**(12)**	(4)
Assets distributed on settlements	**(2)**	(4)
Exchange differences	**9**	(8)
At 31 December	**165**	142
Present value of defined benefit obligations		
At 1 January	**(937)**	(839)
Current service cost	**(12)**	(11)
Interest cost	**(60)**	(55)
Contributions by employees	**(1)**	(2)
Actuarial losses	**(118)**	(44)
Benefits paid	**52**	43
Reduction in liabilities resulting from curtailments	**–**	22
Liabilities extinguished on settlements	**2**	4
Exchange differences	**(13)**	(55)
At 31 December	**(1,087)**	(937)
Funded	**(197)**	(148)
Unfunded	**(890)**	(789)
Unrecognised past service cost	**(24)**	(25)
At 31 December	**(946)**	(820)

The actual return on plan assets for the year ended 31 December 2010 was a positive return of US$19m (2009: positive US$19m).

HSBC expects to make US$61m of contributions to post-employment healthcare benefit plans during 2011. Benefits expected to be paid from the plans to retirees over each of the next five years, and in aggregate for the five years thereafter, are as follows:

Benefits expected to be paid from plans

	2011 US$m	2012 US$m	2013 US$m	2014 US$m	2015 US$m	2016-2020 US$m
Significant plans	57	58	60	62	64	334

Total expense recognised in the income statement in 'Employee compensation and benefits'

	2010 US$m	2009 US$m	2008 US$m
Current service cost	**12**	11	19
Interest cost	**60**	55	65
Expected return on plan assets	**(13)**	(11)	(12)
Past service cost	**(1)**	(2)	(2)
Gains on curtailments	**–**	(22)	(31)
Gains on settlements	**–**	–	(26)
Total expense	**58**	31	13

Summary

	2010 US$m	2009 US$m	2008 US$m	2007 US$m	2006 US$m
Defined benefit obligation	**(1,087)**	(937)	(839)	(1,038)	(1,106)
Fair value of plan assets	**165**	142	128	146	133
Net deficit	**(922)**	(795)	(711)	(892)	(973)
Experience gains/(losses) on plan liabilities	**(27)**	13	(34)	15	(12)
Experience gains/(losses) on plan assets	**6**	8	(14)	(6)	(1)
Gains/(losses) from changes in actuarial assumptions	**(91)**	(57)	32	94	(25)
Total net actuarial gains/(losses)	**(112)**	(36)	(16)	103	(38)

Post-employment defined benefit plans' principal actuarial financial assumptions

The principal actuarial financial assumptions used to calculate the Group's obligations under its defined benefit pension and post-employment healthcare plans at 31 December for each period, and used as the basis for measuring periodic costs under the plans in the following periods, were as follows.

Principal actuarial assumptions

					Healthcare cost trend		
	Discount rate %	**Inflation rate %**	**Rate of increase for pensions[1] %**	**Rate of pay increase %**	**Initial rate %**	**Ultimate rate %**	**Year of ultimate rate**
At 31 December 2010							
UK[2]	**5.40**	**3.70**	**3.50**	**4.20**	**7.70**	**7.70**	**n/a**
Hong Kong	**2.85**	**n/a**	**n/a**	**5.00**	**n/a**	**n/a**	**n/a**
US	**5.41**	**2.50**	**n/a**	**2.75**	**7.20**	**4.50**	**2027**
Jersey	**5.40**	**3.70**	**3.70**	**5.45**	**n/a**	**n/a**	**n/a**
Mexico	**7.50**	**3.50**	**3.50**	**4.50**	**6.75**	**6.75**	**n/a**
Brazil	**10.51**	**4.50**	**4.50**	**5.50**	**10.00**	**5.50**	**2020**
France	**4.75**	**2.00**	**2.00**	**3.00**	**n/a**	**n/a**	**n/a**
Canada	**5.45**	**2.50**	**n/a**	**3.72**	**8.00**	**5.00**	**2015**
Switzerland	**2.60**	**1.50**	**n/a**	**2.50**	**n/a**	**n/a**	**n/a**
Germany	**5.00**	**2.00**	**2.00**	**3.00**	**n/a**	**n/a**	**n/a**
At 31 December 2009							
UK[2]	5.70	3.70	3.50	4.20	7.70	7.70	n/a
Hong Kong	2.58	n/a	n/a	5.00	n/a	n/a	n/a
US	5.92	2.50	n/a	3.50	7.40	4.50	2027
Jersey	5.70	3.70	3.70	5.45	n/a	n/a	n/a
Mexico	8.50	3.50	3.50	4.50	6.75	6.75	n/a
Brazil	11.25	4.50	4.50	5.50	10.00	5.50	2019
France	5.50	2.00	2.00	3.00	n/a	n/a	n/a
Canada	6.25	2.50	n/a	3.72	8.00	5.00	2015
Switzerland	3.25	1.50	n/a	2.50	n/a	n/a	n/a
Germany	5.50	2.00	2.00	3.00	n/a	n/a	n/a

Notes on the Financial Statements (continued)

7 – Employee compensation and benefits

Principal actuarial assumptions (continued)

	Discount rate %	Inflation rate %	Rate of increase for pensions[1] %	Rate of pay increase %	Healthcare cost trend: Initial rate %	Ultimate rate %	Year of ultimate rate
At 31 December 2008							
UK[2]	6.50	2.90	3.00	3.40	6.90	6.90	n/a
Hong Kong	1.19	n/a	n/a	5.00	n/a	n/a	n/a
US	6.05	2.50	n/a	3.50	8.90	5.00	2018
Jersey	6.50	2.90	2.90	4.65	n/a	n/a	n/a
Mexico	8.10	3.50	2.00	4.50	6.75	6.75	n/a
Brazil	10.75	4.50	4.50	5.50	10.00	5.50	2018
France	5.75	2.00	2.00	3.00	n/a	n/a	n/a
Canada	7.19	2.50	n/a	3.85	8.20	4.90	2012
Switzerland	2.60	1.50	n/a	2.39	n/a	n/a	n/a
Germany	5.75	2.00	2.00	3.00	n/a	n/a	n/a

1 *Rate of increase for pensions in payment and deferred pensions (except for the UK).*
2 *Rate of increase for pensions in the UK is for pensions in payment only, capped at 5%. Deferred pensions are projected to increase in line with the assumed inflation rate.*

HSBC determines the discount rates to be applied to its obligations in consultation with the plans' local actuaries, on the basis of current average yields of high quality (AA rated or equivalent) debt instruments, with maturities consistent with those of the defined benefit obligations. In countries where there is not a deep market in corporate bonds, government bond yields have been used. The yield curve has been extrapolated where the term of the liabilities is longer than the duration of available bonds and the discount rate used then takes into account the term of the liabilities and the shape of the yield curve. When determining the discount rate with reference to a bond index, an appropriate index for the specific region has been used.

Mortality tables and average life expectancy at age 65

	Mortality table	Life expectancy at age 65 for a male member currently: Aged 65	Aged 45	Life expectancy at age 65 for a female member currently: Aged 65	Aged 45
At 31 December 2010					
UK	SAPS MC[1]	**22.4**	**24.3**	**23.4**	**25.3**
Hong Kong[4]	n/a	**n/a**	**n/a**	**n/a**	**n/a**
US	RP 2000 fully generational	**19.3**	**20.8**	**21.2**	**22.1**
Jersey	80% of PNA00[2]	**24.2**	**26.2**	**26.6**	**28.5**
Mexico	EMSSA-97 AA generational scale from RP 2000 series	**18.6**	**20.1**	**21.1**	**22.0**
Brazil	RP 2000 fully generational	**19.3**	**20.8**	**21.2**	**22.1**
France	TG 05	**23.4**	**26.1**	**26.8**	**29.7**
Canada	UP94 generational	**19.5**	**21.1**	**22.0**	**22.8**
Switzerland	BVG 2005[3]	**17.9**	**17.9**	**21.0**	**21.0**
Germany	Heubeck 2005 G	**18.4**	**21.1**	**22.5**	**25.1**
At 31 December 2009					
UK	SAPS MC[1]	22.3	24.2	23.3	25.2
Hong Kong[4]	n/a	n/a	n/a	n/a	n/a
US	RP 2000 fully generational	19.2	20.7	21.2	22.1
Jersey	80% of PNA00[2]	24.1	26.1	26.5	28.4
Mexico	EMSSA-97 AA generational scale from RP 2000 series	18.5	20.1	21.1	22.0
Brazil	RP 2000 fully generational	19.2	20.7	21.2	22.1
France	TG 05	23.2	26.0	26.7	29.6
Canada	UP94 generational	19.5	21.1	22.0	22.8
Switzerland	BVG 2005[3]	17.9	17.9	21.0	21.0
Germany	Heubeck 2005 G	18.3	21.0	22.4	25.0

1 *SAPS MC projections with 1% minimum improvement beyond 2002. Light table with 1.08 rating for male and standard table with 1.06 rating for female.*
2 *PNA00 year of birth and medium cohort with 1% minimum improvement thereafter.*
3 *Additional 8.5% liability loading for future mortality improvements.*
4 *The significant plans in Hong Kong are lump sum plans which do not use a post-retirement mortality table.*

Expected rates of return

	2010 Expected rates of return[1] %	2010 Value US$m	2009 Expected rates of return[1] %	2009 Value US$m
HSBC Bank (UK) Pension Scheme				
Fair value of plan assets		**22,236**		17,701
Equities	**8.4**	**3,415**	8.4	2,770
Bonds	**5.3**	**15,638**	5.3	12,597
Property	**7.6**	**1,438**	7.7	1,502
Other	**4.0**	**1,745**	5.3	832
Other plans				
Fair value of plan assets		**7,559**		6,822
Equities	**8.2**	**2,617**	8.2	2,302
Bonds	**5.0**	**4,073**	5.0	3,809
Property	**6.1**	**98**	6.4	55
Other	**6.2**	**771**	3.5	656
Healthcare plans				
Fair value of plan assets		**165**		142
Equities	**12.0**	**49**	12.2	43
Bonds	**8.4**	**81**	8.7	72
Other	**7.6**	**35**	4.6	27

1 *The expected rates of return are used to measure the net defined benefit pension costs in each subsequent year, and weighted on the basis of the fair value of the plan assets.*

The expected return on plan assets represents the best estimate of long-term future asset returns, which takes into account historical market returns plus additional factors such as the current rate of inflation and interest rates.

Actuarial assumption sensitivities

The discount rate is sensitive to changes in market conditions arising during the reporting period. The mortality rates used are sensitive to experience from the plan member profile. The following table shows the effect of changes in these and the other key assumptions on the principal defined benefit pension plan:

The effect of changes in key assumptions on the principal plan

	HSBC Bank (UK) Pension Scheme 2010 US$m	HSBC Bank (UK) Pension Scheme 2009 US$m
Discount rate		
Change in pension obligation at year end from a 25bps increase	**(941)**	(879)
Change in pension obligation at year end from a 25bps decrease	**1,003**	946
Change in 2011 pension cost from a 25bps increase	**(9)**	(13)
Change in 2011 pension cost from a 25bps decrease	**9**	13
Rate of inflation		
Change in pension obligation at year end from a 25bps increase	**1,029**	964
Change in pension obligation at year end from a 25bps decrease	**(978)**	(907)
Change in 2011 pension cost from a 25bps increase	**67**	65
Change in 2011 pension cost from a 25bps decrease	**(64)**	(63)
Rate of increase for pensions in payment and deferred pensions		
Change in pension obligation at year end from a 25bps increase	**813**	800
Change in pension obligation at year end from a 25bps decrease	**(775)**	(766)
Change in 2011 pension cost from a 25bps increase	**48**	50
Change in 2011 pension cost from a 25bps decrease	**(45)**	(49)
Rate of pay increase		
Change in pension obligation at year end from a 25bps increase	**216**	195
Change in pension obligation at year end from a 25bps decrease	**(203)**	(174)
Change in 2011 pension cost from a 25bps increase	**20**	18
Change in 2011 pension cost from a 25bps decrease	**(17)**	(16)
Investment return		
Change in 2011 pension cost from a 25bps increase	**(54)**	(44)
Change in 2011 pension cost from a 25bps decrease	**54**	44
Mortality		
Change in pension obligation from each additional year of longevity assumed	**497**	487

Notes on the Financial Statements (continued)

The effect of changes in the discount rate and in mortality rates on plans other than the principal plan

	Other plans	
	2010	2009
	US$m	US$m
Change in defined benefit obligation at year end from a 25bps increase in discount rate	**(290)**	(269)
Change in 2011 pension cost from a 25bps increase in discount rate	**(1)**	(3)
Increase in defined benefit obligation from each additional year of longevity assumed	**131**	120

Effect of one percentage point change in assumed healthcare cost trend rates

	2010		2009	
	1% increase	**1% decrease**	1% increase	1% decrease
	US$m	**US$m**	US$m	US$m
Increase/(decrease) of the aggregate of the current service cost and interest cost	**8**	**(7)**	8	(7)
Increase/(decrease) of defined benefit obligation	**106**	**(86)**	86	(75)

HSBC Holdings

Employee compensation and benefit expense in respect of HSBC Holdings' employees in 2010 amounted to US$244m (2009: US$217m). The average number of persons employed by HSBC Holdings during 2010 was 1,015 (2009: 876).

Employees of HSBC Holdings who are members of defined benefit pension plans are principally members of either the HSBC Bank (UK) Pension Scheme or the HSBC International Staff Retirement Benefits Scheme.

Directors' emoluments

The aggregate emoluments of the Directors of HSBC Holdings, computed in accordance with the Companies Act 2006 and the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008 were:

	2010	2009	2008
	US$000	US$000	US$000
Fees	**3,597**	3,756	2,529
Salaries and other emoluments	**12,841**	11,835	11,584
Bonuses	**14,294**	–	–
	30,732	15,591	14,113
Gains on the exercise of share options	**–**	–	23
Vesting of Long-Term Incentive awards	**8,523**	1,579	7,147

In addition, there were payments under retirement benefit agreements with former Directors of US$1,016,089 (2009: US$1,036,385). The provision at 31 December 2010 in respect of unfunded pension obligations to former Directors amounted to US$17,628,508 (2009: US$16,296,028).

During the year, aggregate contributions to pension schemes in respect of Directors were US$1,055,582 (2009: US$788,734). Discretionary bonuses for Directors are based on a combination of individual and corporate performance and are determined by the Remuneration Committee. Details of Directors' remuneration, share options and conditional awards under the Restricted Share Plan 2000 and the HSBC Share Plan are included in the 'Directors' Remuneration Report' on pages 232 and 233.

8 Auditors' remuneration

Auditors' remuneration in relation to the statutory audit amounted to US$51.4m (2009: US$50.7m; 2008: US$54.9m). The following fees were payable by HSBC to the Group's principal auditor, KPMG Audit Plc and its associates (together 'KPMG'):

Fees payable by HSBC to KPMG

	2010 US$m	2009 US$m	2008 US$m
Audit fees for HSBC Holdings' statutory audit[1]	**2.4**	2.3	2.1
– fees relating to current year	**2.4**	2.1	2.5
– fees relating to prior year	**–**	0.2	(0.4)
Fees payable to KPMG for other services provided to HSBC	**75.9**	77.1	88.3
Audit-related services:			
– audit of HSBC's subsidiaries, pursuant to legislation[2]	**46.7**	45.9	48.6
– other services pursuant to legislation[3]	**20.8**	24.2	26.5
Tax services[4]	**2.4**	2.6	3.1
Other services:			
– services relating to information technology[5]	**0.1**	0.3	0.6
– services related to corporate finance transactions[6]	**–**	0.1	1.4
– all other services[7]	**5.9**	4.0	8.1
Total fees payable	**78.3**	79.4	90.4

1 *Fees payable to KPMG Audit Plc for the statutory audit of the consolidated financial statements of HSBC and the separate financial statements of HSBC Holdings. They exclude amounts payable for the statutory audit of HSBC Holdings' subsidiaries which have been included in 'Fees payable to KPMG for other services provided to HSBC'.*
2 *Including fees payable to KPMG for the statutory audit of HSBC's subsidiaries.*
3 *Including services for assurance and other services that relate to statutory and regulatory filings, including comfort letters and interim reviews.*
4 *Including tax compliance services and tax advisory services.*
5 *Including advice on IT security and business continuity and performing agreed-upon IT testing procedures.*
6 *Including fees payable to KPMG for transaction-related work, including US debt issuances.*
7 *Including other assurance and advisory services such as translation services, ad-hoc accounting advice and review of financial models.*

No fees were payable by HSBC to KPMG for the following types of services: internal audit services, valuation and actuarial services, services related to litigation and services related to recruitment and remuneration.

Fees payable by HSBC's associated pension schemes to KPMG

	2010 US$000	2009 US$000	2008 US$000
Audit fees	**384**	670	720
Tax services	**–**	–	73
All other services	**–**	260	–
Total fees payable	**384**	930	793

No fees were payable by HSBC's associated pension schemes to KPMG for the following types of services: other services pursuant to legislation, services relating to information technology, internal audit services, valuation and actuarial services, services related to litigation, services related to recruitment and remuneration, and services related to corporate finance transactions.

In addition to the above, KPMG estimate they have been paid fees of US$14.9m (2009: US$8.1m; 2008: US$4.8m) by parties other than HSBC but where HSBC is connected with the contracting party and therefore may be involved in appointing KPMG. These fees arise from services such as auditing mutual funds managed by HSBC and reviewing the financial position of corporate concerns which borrow from HSBC.

Fees payable to KPMG for non-audit services for HSBC Holdings are not disclosed separately because such fees are disclosed on a consolidated basis for HSBC Group.

9 Share-based payments

During 2010, US$813m was charged to the income statement in respect of share-based payment transactions settled in equity (2009: US$683m; 2008: US$819m). This expense, which was computed from the fair values of the share-based payment transactions when contracted, arose under employee share awards made in accordance with HSBC's reward structures.

Calculation of fair values

Fair values of share options/awards, measured at the date of grant of the option/award, are calculated using a Black-Scholes model. When modelling options/awards with vesting dependent on HSBC's Total Shareholder Return ('TSR') over a period, the TSR performance targets are incorporated into the model using Monte Carlo simulation. The expected life of options depends on the behaviour of option holders, which is incorporated into the option model on the basis of historical observable data. The fair values calculated are inherently subjective and uncertain due to the assumptions made and the limitations of the model used.

Significant weighted average assumptions used to estimate the fair value of options granted

	Savings-related share option plans		
	1-year plan	3-year plans	5-year plans
2010			
Risk-free interest rate[1] (%)	**0.7**	**1.9**	**2.9**
Expected life[2] (years)	**1**	**3**	**5**
Expected volatility[3] (%)	**30**	**30**	**30**
Share price at grant date (£)	**6.82**	**6.82**	**6.82**
2009			
Risk-free interest rate[1] (%)	0.7	2.1	2.4
Expected life[2] (years)	1	3	5
Expected volatility[3] (%)	50	35	30
Share price at grant date (£)	4.65	4.65	4.65
2008			
Risk-free interest rate[1] (%)	4.5	4.5	4.5
Expected life[2] (years)	1	3	5
Expected volatility[3] (%)	25	25	25
Share price at grant date (£)	8.80	8.80	8.80

1 *The risk-free rate was determined from the UK gilts yield curve for the UK Savings-Related Share Option Plans. A similar yield curve was used for the International Savings-Related Share Option Plans.*
2 *Expected life is not a single input parameter but a function of various behavioural assumptions.*
3 *Expected volatility is estimated by considering both historic average share price volatility and implied volatility derived from traded options over HSBC shares of similar maturity to those of the employee options.*

The expected US dollar denominated dividend yield was determined to be 4.5% per annum in line with consensus analyst forecasts (2009: 4.5%). Prior to 2009, HSBC adopted a dividend growth model and incorporated expected dividends into the valuation model for share options and awards. In 2008, the expected dividend growth was determined to be 7% for the first year and 8% thereafter.

The HSBC Share Plan

The HSBC Share Plan was approved at the 2005 Annual General Meeting and amendments were approved at the 2008 Annual General Meeting. Under this plan, Performance Share awards, Restricted Share awards and share option awards may be made. The aim of the HSBC Share Plan is to align the interests of executives with the creation of shareholder value and recognise individual performance and potential. Awards are also made under this plan for recruitment and retention purposes.

Performance Share awards

Awards of Performance Shares are made to executive Directors and other senior executives after taking into account individual performance in the previous year. For awards made prior to 2008, each award is divided into two equal parts for testing attainment against pre-determined benchmarks. One half of the award is subject to a TSR measure, based on HSBC's ranking against a comparator group of 28 major banks; the other half is subject to an earnings per share ('EPS') target. For each element of the award, shares are released to the employee on a sliding scale from 30%

to 100% of the award, depending on the scale of achievement against the benchmarks, providing that the minimum criteria for each performance measure have been met.

For awards made during 2008 and prospectively, each award is divided into three parts for testing attainment against pre-determined benchmarks. 40% of the award is subject to a TSR measure, based on a free-float market capitalisation ranking method; 40% is subject to an economic profit measure, calculated as the average annual difference between return on invested capital and HSBC's benchmark cost of capital; and 20% is subject to an EPS target. For the TSR and EPS elements of the awards, shares are released to the employee on a sliding scale from 20% to 100% of the award, depending on the scale of achievement against the benchmarks. For the economic profit element of the awards, shares are released to the employee on a sliding scale from zero to 100%, depending on the scale of achievement against the benchmark. In all cases, shares are only released when the minimum criteria for each performance measure has been met. The performance conditions are measured over a three year performance period and awards forfeited to the extent they have not been met.

In addition to the performance conditions mentioned above, before an award can vest, the Remuneration Committee needs to be satisfied that the Group has shown a sustained improvement in the period since the award was made. In determining this, the Remuneration Committee will take account of all relevant factors, in particular, comparisons against the TSR comparator group in areas such as revenue growth and mix, cost efficiency, credit performance as measured by risk-adjusted revenues, cash return on cash invested, dividend performance and TSR.

Movement in Performance Share awards under the HSBC Share Plan

	2010 Number (000s)	2009 Number (000s)
Outstanding at 1 January	**7,360**	11,619
Additions during the year[1]	**351**	333
Adjustment for rights issue	**–**	1,712
Released in the year	**(1,181)**	(1,076)
Forfeited in the year	**(2,105)**	(5,228)
Outstanding at 31 December	**4,425**	7,360

1 *Additions during the year comprised reinvested dividend equivalents.*

No Performance Shares were awarded by HSBC in 2010 and 2009.

Restricted Share awards

Awards of Restricted Shares are made to employees on the basis of their performance, potential and retention requirements, to aid recruitment or as a part-deferral of annual bonuses. Shares are awarded without corporate performance conditions and generally vest between one and three years from the date of award, providing the employees have remained continually employed by HSBC for this period.

Movement in Restricted Share awards under the HSBC Share Plan

	2010 Number (000s)	2009 Number (000s)
Outstanding at 1 January	**184,318**	122,206
Additions during the year	**110,711**	108,439
Adjustment for rights issue	**–**	26,119
Released in the year	**(55,419)**	(49,718)
Forfeited in the year	**(10,518)**	(22,728)
Outstanding at 31 December	**229,092**	184,318

The weighted average fair value of Restricted Share awards in 2010 was US$10.50 (2009: US$6.31).

Share options

A small number of discretionary share options were granted in 2005 exclusively to individuals employed by HSBC France under the HSBC Share Plan rules, after the expiry of the Group Share Option Plan rules.

Notes on the Financial Statements (continued)

Nil-cost share options were granted to senior executives on the basis of their performance in the previous year. The share options were subject to the achievement of the same corporate performance conditions as the 2005 Performance Share awards. The options vested after three years in the same proportion as the 2005 Performance Shares but were only exercisable up to the fourth anniversary of the date of grant. These options have now lapsed and there are currently no options with outstanding performance conditions.

Share options were also awarded to a number of employees under the HSBC Share Plan rules. These options may vest after three years and are exercisable up to the tenth anniversary of the date of the grant, after which they lapse.

Movement in share options under the HSBC Share Plan

	2010		2009	
	Number (000s)	**Weighted average exercise price £**	Number (000s)	Weighted average exercise price £
Outstanding at 1 January	**86**	**7.99**	300	8.89
Adjustment for rights issue	**–**	**–**	44	7.75
Forfeited and expired in the year	**–**	**–**	(258)	7.66
Outstanding and exercisable at 31 December	**86**	**7.99**	86	7.99

No share options were granted in 2010 and 2009. The weighted average remaining contractual life of options outstanding at the balance sheet date was 4.8 years (2009: 5.8 years). The exercise price of options outstanding at the balance sheet date was £7.99 (2009: £7.99).

Savings-related share option plans

Savings-related share option plans invite eligible employees to enter into savings contracts to save up to £250 per month (or its equivalent in US dollars, Hong Kong dollars or euros), with the option to use the savings to acquire shares. The aim of the plans is to align the interests of all employees with the creation of shareholder value. The options are exercisable within three months following the first anniversary of the commencement of a one-year savings contract or within six months following either the third or the fifth anniversaries of the commencement of three-year or five-year savings contracts, respectively. The exercise price is set at a 20% (2009: 20%) discount to the market value immediately preceding the date of invitation (except for the one-year options granted under the US sub-plan where a 15% discount is applied).

Movement in savings-related share options

	2010		2009	
	Number (000s)	**Weighted average exercise price £**	Number (000s)	Weighted average exercise price £
Outstanding at 1 January	**172,526**	**3.69**	74,401	6.97
Granted in the year	**22,017**	**5.39**	152,796	3.32
Adjustment for rights issue	**–**	**–**	7,970	6.08
Exercised in the year	**(16,830)**	**4.18**	(5,011)	5.72
Forfeited, cancelled and expired in the year	**(19,858)**	**4.44**	(57,630)	5.96
Outstanding at 31 December	**157,855**	**3.87**	172,526	3.69

The weighted average fair value of options granted during the year was US$2.41 (2009: US$2.03). The weighted average share price at the date the share options were exercised was US$10.08 (2009: US$10.23). The exercise price range and weighted average remaining contractual life for options outstanding at the balance sheet date were as follows:

	2010	2009
Exercise price range (£)	**3.31 – 6.69**	3.31 – 6.69
Weighted average remaining contractual life (years)	**2.76**	3.47
Of which exercisable:		
Number (000s)	**1,883**	5,145
Weighted average exercise price (£)	**6.23**	6.26

HSBC Holdings Restricted Share Plan 2000

Restricted Share awards made under the Restricted Share Plan

Awards of Restricted Shares were made under the Restricted Share Plan to eligible employees from 2000 to 2005, after taking into account the employees' performance in the previous year, their potential and retention requirements. Restricted shares were also awarded as part-deferral of annual bonuses or for recruitment purposes. Shares were awarded without corporate performance conditions and in most cases fully vest within three years from the date of award, providing the employees have remained continuously employed by HSBC for the period.

Movement on Restricted Share awards under the HSBC Holdings Restricted Share Plan

	2010 Number (000s)	2009 Number (000s)
Outstanding at 1 January	**173**	2,717
Additions during the year[1]	**–**	30
Adjustment for rights issue	**–**	376
Released in the year	**–**	(2,916)
Forfeited in the year	**(173)**	(34)
Outstanding at 31 December	**–**	173

1 *Additions in 2009 principally comprised reinvested dividend equivalents.*

At 31 December 2009 the weighted average remaining vesting period was 0.3 years.

HSBC Holdings Group Share Option Plan

The HSBC Holdings Group Share Option Plan was a long-term incentive plan under which certain HSBC employees between 2000 and 2005 were awarded share options. The aim of the plan was to align the interests of those higher performing employees with the creation of shareholder value. In most jurisdictions, this was achieved by setting certain TSR targets which would normally have to be attained in order for the awards to vest. Options were granted at market value and are normally exercisable between the third and tenth anniversaries of the date of grant, subject to vesting conditions. Options granted after May 2005 are made under the HSBC Share Plan.

Movement on the HSBC Holdings Group Share Option Plan awards

	2010		2009	
	Number (000s)	Weighted average exercise price £	Number (000s)	Weighted average exercise price £
Outstanding and exercisable at 1 January	**157,719**	**7.12**	142,593	8.16
Adjustment for rights issue	**–**	**–**	21,333	7.12
Exercised in the year	**(1,015)**	**6.08**	(1,548)	6.28
Forfeited and expired in the year	**(3,946)**	**7.36**	(4,659)	7.15
Outstanding and exercisable at 31 December	**152,758**	**7.12**	157,719	7.12

Notes on the Financial Statements (continued)

9 – Share-based payments / 10 – Tax expense

The weighted average share price at the date the share options were exercised was US$10.26 (2009: US$9.14). The number of options, weighted average exercise price and weighted average remaining contractual life of options outstanding at the balance sheet date, analysed by exercise price range, were as follows:

	2010		2009	
Exercise price range (£)	**6.00 – 7.00**	**7.01 – 8.50**	6.00 – 7.00	7.01 – 8.50
Number (000s)	**26,927**	**125,831**	28,406	129,313
Weighted average exercise price (£)	**6.03**	**7.36**	6.03	7.36
Weighted average remaining contractual life (years)	**2.33**	**2.34**	3.33	3.34
Of which exercisable:				
Number (000s)	**26,927**	**125,831**	28,406	129,313
Weighted average exercise price (£)	**6.03**	**7.36**	6.03	7.36

HSBC Holdings Executive Share Option Scheme

The HSBC Holdings Executive Share Option Scheme was a long-term incentive plan under which certain senior HSBC employees were awarded share options before the adoption of the HSBC Holdings Group Share Option Plan in 2000. The aim of the plan was to align the interests of those higher performing senior employees with the creation of shareholder value. This was achieved by setting certain TSR targets to be attained in order for the awards to vest. Options were granted at market value and were exercisable between the third and tenth anniversaries of the date of grant, subject to vesting conditions. No awards have been made under this plan since 2000 and all options have now expired or been exercised.

Movement on the HSBC Holdings Executive Share Option Scheme awards

	2010		2009	
	Number (000s)	**Weighted average exercise price £**	Number (000s)	Weighted average exercise price £
Outstanding and exercisable at 1 January	**6,707**	**6.50**	13,964	6.92
Adjustment for rights issue	**–**	**–**	2,046	6.04
Exercised in the year	**(4,229)**	**6.50**	(920)	6.39
Expired in the year	**(2,478)**	**6.50**	(8,383)	5.61
Outstanding and exercisable at 31 December	**–**	**–**	6,707	6.50

The weighted average share price at the date the share options were exercised was US$10.26 (2009: US$9.14).

At 31 December 2009, the exercise price range for options outstanding was £5.50–£7.00 and the weighted average remaining contractual life of options outstanding was 0.26 years.

HSBC France and subsidiary company plans

Before its acquisition by HSBC in 2000, HSBC France and certain of its subsidiaries operated employee share option plans. Options over HSBC France shares granted between 1994 and 1999 vested upon announcement of HSBC's agreement to acquire HSBC France and were therefore included in the valuation of HSBC France.

HSBC France granted 909,000 options in 2000 after the public announcement of the acquisition. The options vested on 1 January 2002. The HSBC France shares obtained on exercise of the options were exchangeable for HSBC Holdings ordinary shares of US$0.50. Options were granted at market value and are exercisable within ten years of the date of grant. Movements in options granted after the public announcement are shown below.

Movement on HSBC France share options

	2010		2009	
	Number (000s)	**Exercise price €**	Number (000s)	Exercise price €
Outstanding and exercisable at 1 January	**604**	**142.5**	604	142.5
Forfeited in the year	**(604)**	**142.5**	–	–
Outstanding and exercisable at 31 December	**–**	**–**	604	142.5

At 31 December 2009, the remaining contractual life for options outstanding was 0.3 years.

At the date of its acquisition, certain of HSBC France's subsidiary companies also operated employee share option plans. On exercise of certain of these options, the subsidiary shares are exchanged for HSBC ordinary shares. The total number of HSBC ordinary shares exchanged under such arrangements in 2010 was 9,281 (2009: 70,257).

HSBC Finance

Upon acquisition, HSBC Finance share options previously granted were converted to share options over HSBC ordinary shares of US$0.50 each at a rate of 2.675 HSBC share options (the same ratio as the Exchange Offer for HSBC Finance) for each HSBC Finance share option. Options granted under HSBC Finance's own share option schemes prior to the announcement of the acquisition by HSBC in November 2002 vested as options over HSBC shares upon acquisition by HSBC. Options granted after the announcement of the acquisition but prior to its completion on 28 March 2003 generally vest equally over four years and expire ten years from the date of grant. Options granted after the announcement are shown in the table below.

Movement on HSBC Finance share options

	2010		2009	
	Number (000s)	**Exercise price US$**	Number (000s)	Exercise price US$
Outstanding at 1 January	**2,736**	**9.29**	2,402	10.66
Adjustment for rights issue	**–**	**–**	354	9.29
Exercised in the year	**(307)**	**9.29**	(20)	9.29
Expired in the year	**–**	**–**	–	9.29
Outstanding and exercisable at 31 December	**2,429**	**9.29**	2,736	9.29

The weighted average share price at the date the share options were exercised was US$10.26 (2009: US$9.14). The remaining contractual life for options outstanding at the balance sheet date was 1.9 years (2009: 2.9 years).

10 Tax expense

	2010 US$m	2009 US$m	2008 US$m
Current tax			
UK Corporation tax	**383**	206	1,671
– on current year profit	**404**	280	1,738
– adjustments in respect of prior years	**(21)**	(74)	(67)
Overseas tax	**3,328**	1,847	1,703
– on current year profit	**3,235**	1,826	1,732
– adjustments in respect of prior years	**93**	21	(29)
	3,711	2,053	3,374
Deferred tax			
Origination and reversal of temporary differences	**1,176**	(1,672)	(504)
Effect of changes in tax rates	**31**	(10)	(89)
Adjustments in respect of prior years	**(72)**	14	28
	1,135	(1,668)	(565)
Tax expense	**4,846**	385	2,809

The UK corporation tax rate applying to HSBC Holdings and its subsidiaries was 28% (2009: 28%; 2008: 30% to 31 March 2008 and 28% thereafter). Overseas tax included Hong Kong profits tax of US$962m (2009: US$783m; 2008: US$846m). The Hong Kong tax rate applying to the profits of subsidiaries assessable in Hong Kong was 16.5% (2009: 16.5%; 2008: 16.5%). Other overseas subsidiaries and overseas branches provided for taxation at the appropriate rates in the countries in which they operate.

Notes on the Financial Statements (continued)

10 – Tax expense

The following table reconciles the tax expense which would apply if all profits had been taxed at the UK corporation tax rate:

Analysis of tax expense

	2010		2009		2008	
	US$m	%	US$m	%	US$m	%
Taxation at UK corporation tax rate of 28% (2009: 28%; 2008: 28.5%)[1]	**5,330**	**28.0**	1,982	28.0	2,652	28.5
Goodwill impairment	**–**	**–**	–	–	3,010	32.3
Non-deductible loss on foreign exchange swaps on rights issue proceeds[2]	**–**	**–**	96	1.4	–	–
Effect of taxing overseas profits in principal locations at different rates	**(744)**	**(3.9)**	(1,345)	(19.0)	(1,339)	(14.4)
Gains not subject to tax	**(275)**	**(1.4)**	(238)	(3.4)	(1,016)	(10.9)
Adjustments in respect of prior period liabilities	**–**	**–**	(39)	(0.6)	(67)	(0.7)
Low income housing tax credits[3]	**(86)**	**(0.5)**	(98)	(1.4)	(103)	(1.1)
Effect of profit in associates and joint ventures	**(705)**	**(3.7)**	(499)	(7.1)	(473)	(5.1)
Tax impact of intra-group transfer of subsidiary[4]	**1,216**	**6.4**	–	–	–	–
Impact of gains arising from dilution of interests in associates	**(53)**	**(0.3)**	–	–	–	–
Deferred tax temporary differences not provided/(previously not recognised)[5]	**(6)**	**–**	360	5.1	157	1.7
Non taxable income	**(374)**	**(2.0)**	(365)	(5.2)	(519)	(5.6)
Permanent disallowables	**276**	**1.5**	223	3.2	217	2.3
Additional provision for tax on overseas dividends	**–**	**–**	341	4.8	294	3.2
Effect of bank payroll tax	**79**	**0.4**	–	–	–	–
Change in tax rates	**31**	**0.2**	(10)	(0.1)	(89)	(0.9)
Local taxes and overseas withholding tax	**61**	**0.3**	12	0.1	122	1.3
Other items	**96**	**0.5**	(35)	(0.4)	(37)	(0.4)
Tax expense[1]	**4,846**	**25.5**	385	5.4	2,809	30.2

1 *The change in the UK corporation tax rate from 30% to 28% with effect from 1 April 2008 gave rise to a blended tax rate for 2008 of 28.5%.*
2 *In August 2009, the UK Government enacted legislation that gains or losses on transactions designated to hedge foreign exchange exposures connected to rights issues should be disregarded for tax purposes.*
3 *Low income housing tax credits arise in the US and are designed to encourage the provision of rental housing for low income households.*
4 *This relates to the transfer of HSBC Bank Canada, which was part of the sub-group headed by HSBC North America Holdings Inc, to HSBC Overseas Holdings (UK) Limited. A taxable gain arises on this disposal but the crystallisation of deferred tax assets and utilisation of current year foreign tax credits meant that no tax was paid on this transfer.*
5 *2009 and 2008 include the effect of previously unrecognised temporary differences principally related to the recognition of foreign tax credits and trading losses, respectively.*

On 22 June 2010, the UK Government announced its intention to reduce the main rate of corporation tax from 28% to 24%. It is proposed that the reduction will be phased in over a period of four years with a 1% decrease in the main corporation tax rate for each year starting on 1 April 2011. As at 31 December 2010, only the initial phase to reduce the main rate of UK corporation tax from 28% to 27% has been substantively enacted and therefore only this change has been reflected in the amounts recognised as at that date. However, it is not expected that the future proposed rate changes will have a significant effect on the net UK deferred tax asset recognised at 31 December 2010 of US$383m.

Deferred taxation

The following table shows the deferred tax assets and liabilities before offsetting balances within countries and the related movements recognised in the income statement, other comprehensive income and directly in equity.

Movement of deferred tax assets and liabilities before offsetting balances within countries

2010	Retirement benefits US$m	Loan impairment allowances US$m	Unused tax losses US$m	Accelerated capital allowances US$m	Available-for-sale investments US$m	Cash flow hedges US$m	Share-based payments US$m	Assets leased to customers US$m	Revaluation of property US$m	Fee income US$m	Relief for unused tax credits US$m	Other US$m	Total US$m
Assets	**1,772**	**6,363**	**164**	**215**	**68**	**229**	**196**	**–**	**–**	**–**	**243**	**1,535**	**10,785**
Liabilities	**–**	**–**	**–**	**(129)**	**(340)**	**(91)**	**–**	**(1,121)**	**(399)**	**(1,080)**	**–**	**(842)**	**(4,002)**
At 1 January 2010	**1,772**	**6,363**	**164**	**86**	**(272)**	**138**	**196**	**(1,121)**	**(399)**	**(1,080)**	**243**	**693**	**6,783**
Acquisitions and disposals	**–**	**8**	**–**	**–**	**12**	**(2)**	**–**	**–**	**–**	**–**	**–**	**(16)**	**2**
Income statement	**(468)**	**(1,702)**	**2**	**14**	**(16)**	**3**	**50**	**250**	**75**	**386**	**(72)**	**343**	**(1,135)**
Other comprehensive income:													
– available-for-sale investment	**–**	**–**	**–**	**–**	**(73)**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(73)**
– cash flow hedges	**–**	**–**	**–**	**–**	**–**	**70**	**–**	**–**	**–**	**–**	**–**	**–**	**70**
– actuarial losses	**(1)**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(1)**
Equity:													
– share-based payments	**–**	**–**	**–**	**–**	**–**	**–**	**(14)**	**–**	**–**	**–**	**–**	**–**	**(14)**
Foreign exchange and other adjustments	**235**	**130**	**15**	**(117)**	**225**	**55**	**9**	**164**	**99**	**(62)**	**(4)**	**(463)**	**286**
At 31 December 2010	**1,538**	**4,799**	**181**	**(17)**	**(124)**	**264**	**241**	**(707)**	**(225)**	**(756)**	**167**	**557**	**5,918**
Assets	**1,538**	**4,799**	**181**	**109**	**11**	**352**	**241**	**–**	**–**	**–**	**170**	**957**	**8,358**
Liabilities	**–**	**–**	**–**	**(126)**	**(135)**	**(88)**	**–**	**(707)**	**(225)**	**(756)**	**(3)**	**(400)**	**(2,440)**
2009													
Assets	927	5,891	282	99	518	1,145	245	–	–	–	94	363	9,564
Liabilities	–	–	–	(167)	(121)	(280)	–	(916)	(374)	(930)	–	(1,620)	(4,408)
At 1 January 2009	927	5,891	282	(68)	397	865	245	(916)	(374)	(930)	94	(1,257)	5,156
Acquisitions and disposals	–	–	–	–	–	–	–	–	–	–	–	–	–
Income statement	(193)	19	(141)	132	(33)	(4)	(82)	136	29	3	414	1,388	1,668
Other comprehensive income:													
– available-for-sale investment	–	–	–	–	(587)	–	–	–	–	–	–	–	(587)
– cash flow hedges	–	–	–	–	–	(517)	–	–	–	–	–	–	(517)
– actuarial losses	978	–	–	–	–	–	–	–	–	–	–	–	978
Equity:													
– share-based payments	–	–	–	–	–	–	9	–	–	–	–	–	9
Foreign exchange and other adjustments	60	453	23	22	(49)	(206)	24	(341)	(54)	(153)	(265)	562	76
At 31 December 2009	1,772	6,363	164	86	(272)	138	196	(1,121)	(399)	(1,080)	243	693	6,783
Assets	1,772	6,363	164	215	68	229	196	–	–	–	243	1,535	10,785
Liabilities	–	–	–	(129)	(340)	(91)	–	(1,121)	(399)	(1,080)	–	(842)	(4,002)

Presentation of deferred tax balances

Deferred tax balances are presented in the consolidated balance sheet after offsetting asset and liability balances where HSBC has the legal right to set off and intends to settle on a net basis, as follows:

	2010 US$m	2009 US$m
Deferred tax assets	**7,011**	8,620
Deferred tax liabilities	**(1,093)**	(1,837)
	5,918	6,783

Analysis of deferred tax assets by country

	2010 US$m	2009 US$m
US	**4,043**	5,110
Brazil	**883**	1,289
Mexico	**665**	620
UK	**383**	395
Other	**1,037**	1,206
	7,011	8,620

The amount of temporary differences, unused tax losses and unused tax credits excluding the US, for which no deferred tax asset is recognised in the balance sheet is US$2,473m (2009: US$1,723m). Of this amount, US$2,366m (2009: US$1,608m) has no expiry date, US$107m (2009: US$115m) is scheduled to expire within 10 years (2009: 10 years) and the remaining will expire after 10 years. The deferred tax asset unrecognised in respect of these items is US$601m (2009: US$491m), of which US$564m (2009: US$450m) has no expiry date, US$37m (2009: US$40m) is scheduled to expire within 10 years (2009: 10 years) and the remaining will expire after 10 years.

In the US, the deferred tax asset unrecognised in respect of temporary differences, unused tax losses and unused tax credits was US$1,715m (2009: US$1,577m), of which US$70m (2009: US$52m) has no expiry date, US$908m (2009: US$932m) is scheduled to expire within 10 years (2009: 10 years) and the remaining will expire within 20 years.

The US deferred tax assets not recognised of US$1,715m (2009: US$1,577m) comprise unused state losses of US$694m (2009: US$854m), unused federal losses of US$43m (2009: nil), unused tax credits of US$908m (2009: US$716m) and other differences of US$70m (2009: US$7m). The gross temporary difference in respect of the unused state losses is US$12,486m (2009: US$15,517m), the unused federal losses are US$122m (2009: nil), the other differences are US$200m (2009: US$20m), while no gross equivalent is applied to the unused tax credits.

Deferred tax of US$89m (2009: US$94m) has been provided in respect of distributable reserves of associates that, on distribution, would attract withholding tax.

Deferred tax is not recognised in respect of the Group's investments in subsidiaries and branches where remittance is not contemplated, and for those associates and interests in joint ventures where it has been determined that no additional tax will arise. The aggregate amount of temporary differences associated with investments where no deferred tax liability is recognised is nil (2009: nil; 2008: US$38,443m). Following the change in the UK tax treatment of dividends on 1 July 2009, no UK tax is expected to arise on distributions from group entities and no temporary difference exists except where withholding tax or other foreign tax could arise on the investments. No amount is disclosed for the unrecognised deferred tax or the 2010 and 2009 temporary differences associated with such investments, as it is impracticable to determine the amount of income taxes that would be payable when any temporary differences reverse.

Of the total net deferred tax assets of US$7.0bn at 31 December 2010 (2009: US$8.6bn), US$4.0bn (2009: US$5.1bn) arose in respect of HSBC's US operations where there has been a recent history of losses. Management's analysis of the recognition of these deferred tax assets significantly discounts any future expected profits from the US operations and relies to a greater extent on capital support to the US operations from HSBC Holdings plc, including tax planning strategies implemented in relation to such support. Further to the implementation of this strategy, the transfer of HSBC Bank Canada, which was part of the sub-group headed by HSBC North America Holdings Inc., to HSBC Overseas Holdings (UK) Limited in an internal reorganisation on 31 January 2010, provided substantial support for the recoverability of the US deferred tax assets. The associated taxable gain arising in the US operations reduced the deferred tax assets by US$1.2bn. US legislation enacted on 6 November 2009 allowed for an extended carryback period for certain federal tax net operating losses. This had the effect of crystallising deferred tax assets related to such losses at 31 December 2009 by approximately US$1.6bn. Currently, it has been determined that the US operations primary tax planning strategy, in combination with other tax planning strategies, provides support for the realisation of the net deferred tax assets recorded for the US operations. Such determination is based on HSBC's business forecasts and assessments as to the most efficient and effective deployment of HSBC capital, most importantly including the length of time such capital will need to be maintained in the US for purposes of the tax planning strategy.

The deferred tax assets relating to HSBC's Brazil operation is US$0.9bn (2009: US$1.3bn) and the Mexican operation is US$0.7bn (2009: US$0.6bn). On the evidence available, including management projections of income and the state of the Brazilian and Mexican economies, there will be sufficient taxable income generated by the businesses to support these assets.

HSBC Holdings

	Deferred tax assets/(liabilities)	
	2010	2009
	US$m	US$m
Temporary differences:		
– short-term timing differences	**1**	1
– available-for-sale investments	**(21)**	(99)
– fair valued assets and liabilities	**61**	76
– share-based payments	**16**	8
	57	(14)

11 Dividends

Dividends to shareholders of the parent company

	2010			2009			2008		
	Per share US$	**Total US$m**	**Settled in scrip US$m**	Per share US$	Total US$m	Settled in scrip US$m	Per share US$	Total US$m	Settled in scrip US$m
Dividends declared on ordinary shares									
In respect of previous year:									
– fourth interim dividend	**0.10**	**1,733**	**838**	0.10	1,210	624	0.39	4,620	2,233
In respect of current year:									
– first interim dividend	**0.08**	**1,394**	**746**	0.08	1,384	190	0.18	2,158	256
– second interim dividend	**0.08**	**1,402**	**735**	0.08	1,385	696	0.18	2,166	727
– third interim dividend	**0.08**	**1,408**	**205**	0.08	1,391	160	0.18	2,175	380
	0.34	**5,937**	**2,524**	0.34	5,370	1,670	0.93	11,119	3,596
Quarterly dividends on preference shares classified as equity									
March dividend	**15.50**	**22**		15.50	22		15.50	22	
June dividend	**15.50**	**23**		15.50	23		15.50	23	
September dividend	**15.50**	**22**		15.50	22		15.50	22	
December dividend	**15.50**	**23**		15.50	23		15.50	23	
	62.00	**90**		62.00	90		62.00	90	
Quarterly coupons on capital securities classified as equity[1]									
January coupon	**0.508**	**44**		0.508	44		–	–	
April coupon	**0.508**	**45**		0.508	45		–	–	
July coupon	**0.508**	**45**		0.508	45		0.541	47	
September coupon	**0.450**	**68**		–	–		–	–	
October coupon	**0.508**	**45**		0.508	45		0.508	45	
December coupon	**0.500**	**76**		–	–		–	–	
	2.982	**323**		2.032	179		1.049	92	

1 *HSBC Holdings issued Perpetual Subordinated Capital Securities of US$3,800m in June 2010 and US$2,200m in April 2008, which are classified as equity under IFRSs.*

The Directors declared after the end of the year a fourth interim dividend in respect of the financial year ended 31 December 2010 of US$0.12 per ordinary share, a distribution of approximately US$2,125m. The fourth interim dividend will be payable on 5 May 2011 to holders of record on 17 March 2011 on the Hong Kong Overseas Branch Register and 18 March 2011 on the Principal Register in the UK or the Bermuda Overseas Branch Register. No liability is recorded in the financial statements in respect of the fourth interim dividend for 2010.

On 18 January 2011, HSBC paid a further coupon on the capital securities of US$0.508 per security, a distribution of US$44m. No liability is recorded in the balance sheet at 31 December 2010 in respect of this coupon payment.

12 Earnings per share

Basic earnings per ordinary share was calculated by dividing the profit attributable to ordinary shareholders of the parent company by the weighted average number of ordinary shares outstanding, excluding own shares held. Diluted earnings per ordinary share was calculated by dividing the basic earnings, which require no adjustment for the effects of dilutive potential ordinary shares, by the weighted average number of ordinary shares outstanding, excluding own shares held, plus the weighted average number of ordinary shares that would be issued on conversion of dilutive potential ordinary shares.

Profit attributable to the ordinary shareholders of the parent company

	2010 US$m	2009 US$m	2008 US$m
Profit attributable to shareholders of the parent company	**13,159**	5,834	5,728
Dividend payable on preference shares classified as equity	**(90)**	(90)	(90)
Coupon payable on capital securities classified as equity	**(323)**	(179)	(92)
Profit attributable to the ordinary shareholders of the parent company	**12,746**	5,565	5,546

Basic and diluted earnings per share

	2010			2009			2008		
	Profit US$m	**Number of shares (millions)**	**Per share US$**	Profit US$m	Number of shares (millions)	Per share US$	Profit US$m	Number of shares (millions)	Per share US$
Basic[1]	**12,746**	**17,404**	**0.73**	5,565	16,277	0.34	5,546	13,555	0.41
Effect of dilutive potential ordinary shares		**229**			143			118	
– Savings-related Share Option Plan		**55**			26			13	
– Executive Share Option Scheme		**–**			–			3	
– Group Share Option Plan		**–**			–			5	
– Restricted and performance share awards		**174**			117			95	
– HSBC France share options		**–**			–			1	
– HSBC Finance share options		**–**			–			1	
Diluted[2]	**12,746**	**17,633**	**0.72**	5,565	16,420	0.34	5,546	13,673	0.41

1 *Weighted average number of ordinary shares outstanding.*
2 *Weighted average number of ordinary shares outstanding assuming dilution.*

The weighted average number of dilutive potential ordinary shares excludes 150m employee share options that were anti-dilutive (2009: 214m; 2008: 166m).

13 Segmental analysis

HSBC's operating segments are organised into six geographical regions, Europe, Hong Kong, Rest of Asia-Pacific, Middle East, North America and Latin America. Due to the nature of the Group, HSBC's chief operating decision-maker regularly reviews operating activity on a number of bases, including by geographical region, customer group and global business and retail businesses by geographical region. The segmental analysis is presented on a geographical basis because, although information is reviewed on a number of bases, capital resources are allocated and performance is assessed primarily by geographical region. Also, the economic conditions of each geographical region are highly influential in determining the performance of the different businesses carried out in each region. As a result, provision of segmental information on a geographical basis provides the most meaningful basis from which to assess performance. HSBC's chief operating decision-maker is the Group Management Board which operates as a general management committee under the direct authority of the Board.

Geographical information is classified by the location of the principal operations of the subsidiary or, for The Hongkong and Shanghai Banking Corporation, HSBC Bank, HSBC Bank Middle East and HSBC Bank USA, by the location of the branch responsible for reporting the results or advancing the funds.

Information provided to HSBC's chief operating decision-maker to make decisions about allocating resources to, and assessing the performance of, operating segments is measured in accordance with IFRSs. The financial information shown below includes the effects of intra-HSBC transactions between operating segments which are conducted on an arm's length basis and eliminated in a separate column. Shared costs are included in operating segments on the basis of the actual recharges made.

Products and services

HSBC provides a comprehensive range of banking and related financial services to its customers in its six geographical regions. The products and services offered to customers are organised by customer group and global business.

- Personal Financial Services offers a broad range of products and services to meet the personal banking, consumer finance and wealth management needs of individual customers. Personal banking products typically include current and savings accounts, mortgages and personal loans, credit cards, debit cards, insurance, wealth management and local and international payment services.
- Commercial Banking product offerings include the provision of financing services, payments and cash management, international trade finance, treasury and capital markets, commercial cards, insurance, and online and direct banking offerings.
- Global Banking and Markets provides tailored financial solutions to major government, corporate and institutional clients and private investors worldwide. The client-focused business lines deliver a full range of banking capabilities including financing, advisory and transaction services; a markets business that provides services in credit, rates, foreign exchange, money markets and securities services; global asset management services and principal investment activities.
- Global Private Banking provides a range of services to meet the banking, investment and wealth advisory needs of high net worth individuals.

Financial information

In the following segmental analysis, the benefit of shareholders' funds impacts the analysis only to the extent that these funds are actually allocated to businesses in the segment by way of intra-HSBC capital and funding structures.

Notes on the Financial Statements (continued)

13 – Segmental analysis

Profit/(loss) for the year

	2010							
	Europe US$m	Hong Kong US$m	Rest of Asia-Pacific US$m	Middle East US$m	North America US$m	Latin America US$m	Intra-HSBC items US$m	Total US$m
Interest income	17,550	5,102	6,432	2,003	16,781	11,590	(1,113)	58,345
Interest expense	(6,300)	(856)	(2,604)	(636)	(4,342)	(5,279)	1,113	(18,904)
Net interest income	11,250	4,246	3,828	1,367	12,439	6,311	–	39,441
Fee income	8,334	3,460	2,399	737	4,524	2,366	(703)	21,117
Fee expense	(1,963)	(498)	(467)	(60)	(860)	(617)	703	(3,762)
Net fee income	6,371	2,962	1,932	677	3,664	1,749	–	17,355
Trading income excluding net interest income	1,461	1,107	1,207	343	109	453	–	4,680
Net interest income on trading activities	1,402	205	411	27	205	280	–	2,530
Net trading income	2,863	1,312	1,618	370	314	733	–	7,210
Changes in fair value of long-term debt issued and related derivatives	(365)	(2)	(2)	–	111	–	–	(258)
Net income from other financial instruments designated at fair value	647	380	26	–	–	425	–	1,478
Net income from financial instruments designated at fair value	282	378	24	–	111	425	–	1,220
Gains less losses from financial investments	486	98	146	(3)	143	98	–	968
Dividend income	20	30	1	7	42	12	–	112
Net earned insurance premiums	4,067	4,332	448	–	245	2,054	–	11,146
Other operating income/(expense)	2,117	1,606	1,598	(8)	233	141	(3,125)	2,562
Total operating income	27,456	14,964	9,595	2,410	17,191	11,523	(3,125)	80,014
Net insurance claims incurred and movement in liabilities to policyholders	(4,706)	(4,762)	(363)	–	(144)	(1,792)	–	(11,767)
Net operating income before loan impairment charges and other credit risk provisions	22,750	10,202	9,232	2,410	17,047	9,731	(3,125)	68,247
Loan impairment charges and other credit risk provisions	(3,020)	(114)	(439)	(627)	(8,295)	(1,544)	–	(14,039)
Net operating income	19,730	10,088	8,793	1,783	8,752	8,187	(3,125)	54,208
Employee compensation and benefits	(7,875)	(2,341)	(2,719)	(579)	(3,672)	(2,650)	–	(19,836)
General and administrative expenses	(6,499)	(1,686)	(2,181)	(450)	(4,179)	(3,286)	3,125	(15,156)
Depreciation and impairment of property, plant and equipment	(719)	(237)	(189)	(42)	(288)	(238)	–	(1,713)
Amortisation and impairment of intangible assets	(352)	(167)	(54)	(7)	(183)	(220)	–	(983)
Total operating expenses	(15,445)	(4,431)	(5,143)	(1,078)	(8,322)	(6,394)	3,125	(37,688)
Operating profit	4,285	5,657	3,650	705	430	1,793	–	16,520
Share of profit in associates and joint ventures	17	35	2,252	187	24	2	–	2,517
Profit before tax	4,302	5,692	5,902	892	454	1,795	–	19,037
Tax expense	(1,006)	(987)	(962)	(138)	(1,180)	(573)	–	(4,846)
Profit/(loss) for the year	3,296	4,705	4,940	754	(726)	1,222	–	14,191

	2009							
	Europe US$m	Hong Kong US$m	Rest of Asia-Pacific US$m	Middle East US$m	North America US$m	Latin America US$m	Intra-HSBC items US$m	Total US$m
Interest income	20,283	5,327	5,877	2,260	19,526	10,091	(1,268)	62,096
Interest expense	(8,015)	(1,132)	(2,338)	(775)	(5,856)	(4,518)	1,268	(21,366)
Net interest income	12,268	4,195	3,539	1,485	13,670	5,573	–	40,730
Fee income	8,576	3,099	1,972	682	5,496	2,230	(652)	21,403
Fee expense	(2,309)	(430)	(415)	(57)	(679)	(501)	652	(3,739)
Net fee income	6,267	2,669	1,557	625	4,817	1,729	–	17,664
Trading income excluding net interest income	2,861	1,068	1,264	369	35	639	–	6,236
Net interest income on trading activities	2,598	157	342	25	296	209	–	3,627
Net trading income	5,459	1,225	1,606	394	331	848	–	9,863
Changes in fair value of long-term debt issued and related derivatives	(2,746)	(3)	(1)	–	(3,497)	–	–	(6,247)
Net income from other financial instruments designated at fair value	1,321	788	111	–	1	495	–	2,716
Net income/(expense) from financial instruments designated at fair value	(1,425)	785	110	–	(3,496)	495	–	(3,531)
Gains less losses from financial investments	50	9	(19)	16	296	168	–	520
Dividend income	29	28	2	3	53	11	–	126
Net earned insurance premiums	4,223	3,674	365	–	309	1,900	–	10,471
Other operating income	2,262	1,274	1,238	71	566	133	(2,756)	2,788
Total operating income	29,133	13,859	8,398	2,594	16,546	10,857	(2,756)	78,631
Net insurance claims incurred and movement in liabilities to policyholders	(5,589)	(4,392)	(395)	–	(241)	(1,833)	–	(12,450)
Net operating income before loan impairment charges and other credit risk provisions	23,544	9,467	8,003	2,594	16,305	9,024	(2,756)	66,181
Loan impairment charges and other credit risk provisions	(5,568)	(500)	(896)	(1,334)	(15,664)	(2,526)	–	(26,488)
Net operating income	17,976	8,967	7,107	1,260	641	6,498	(2,756)	39,693
Employee compensation and benefits	(7,174)	(2,102)	(2,363)	(545)	(4,085)	(2,199)	–	(18,468)
General and administrative expenses	(5,775)	(1,502)	(1,872)	(419)	(3,794)	(2,786)	2,756	(13,392)
Depreciation and impairment of property, plant and equipment	(762)	(224)	(172)	(31)	(329)	(207)	–	(1,725)
Amortisation and impairment of intangible assets	(277)	(118)	(43)	(6)	(183)	(183)	–	(810)
Total operating expenses	(13,988)	(3,946)	(4,450)	(1,001)	(8,391)	(5,375)	2,756	(34,395)
Operating profit/(loss)	3,988	5,021	2,657	259	(7,750)	1,123	–	5,298
Share of profit in associates and joint ventures	21	8	1,543	196	12	1	–	1,781
Profit/(loss) before tax	4,009	5,029	4,200	455	(7,738)	1,124	–	7,079
Tax income/(expense)	(776)	(869)	(753)	(94)	2,285	(178)	–	(385)
Profit/(loss) for the year	3,233	4,160	3,447	361	(5,453)	946	–	6,694

Notes on the Financial Statements (continued)

13 – Segmental analysis

Profit/(loss) for the year (continued)

	2008							
	Europe US$m	Hong Kong US$m	Rest of Asia-Pacific US$m	Middle East US$m	North America US$m	Latin America US$m	Intra-HSBC items US$m	Total US$m
Interest income	35,117	9,530	9,066	2,451	25,897	11,632	(2,392)	91,301
Interest expense	(25,421)	(3,832)	(5,129)	(895)	(10,679)	(5,174)	2,392	(48,738)
Net interest income	9,696	5,698	3,937	1,556	15,218	6,458	–	42,563
Fee income	10,225	3,062	2,414	740	6,292	2,716	(685)	24,764
Fee expense	(2,733)	(482)	(547)	(49)	(1,065)	(549)	685	(4,740)
Net fee income	7,492	2,580	1,867	691	5,227	2,167	–	20,024
Trading income/(expense) excluding net interest income	1,691	856	1,443	380	(3,879)	356	–	847
Net interest income on trading activities	3,666	337	599	22	744	345	–	5,713
Net trading income/(expense)	5,357	1,193	2,042	402	(3,135)	701	–	6,560
Changes in fair value of long-term debt issued and related derivatives	2,939	3	1	–	3,736	–	–	6,679
Net income/(expense) from other financial instruments designated at fair value	(1,826)	(1,194)	(172)	–	1	364	–	(2,827)
Net income/(expense) from financial instruments designated at fair value	1,113	(1,191)	(171)	–	3,737	364	–	3,852
Gains less losses from financial investments	418	(309)	24	8	(120)	176	–	197
Dividend income	130	41	2	2	77	20	–	272
Net earned insurance premiums	5,299	3,247	197	–	390	1,717	–	10,850
Gains on disposal of French regional banks	2,445	–	–	–	–	–	–	2,445
Other operating income	2,096	817	1,055	9	23	300	(2,492)	1,808
Total operating income	34,046	12,076	8,953	2,668	21,417	11,903	(2,492)	88,571
Net insurance claims incurred and movement in liabilities to policyholders	(3,367)	(1,922)	28	–	(238)	(1,390)	–	(6,889)
Net operating income before loan impairment charges and other credit risk provisions	30,679	10,154	8,981	2,668	21,179	10,513	(2,492)	81,682
Loan impairment charges and other credit risk provisions	(3,754)	(765)	(852)	(279)	(16,795)	(2,492)	–	(24,937)
Net operating income	26,925	9,389	8,129	2,389	4,384	8,021	(2,492)	56,745
Employee compensation and benefits	(8,551)	(2,069)	(2,475)	(544)	(4,609)	(2,544)	–	(20,792)
General and administrative expenses	(6,428)	(1,562)	(2,037)	(384)	(4,282)	(3,059)	2,492	(15,260)
Depreciation and impairment of property, plant and equipment	(865)	(209)	(163)	(25)	(265)	(223)	–	(1,750)
Amortisation and impairment of intangible assets	(228)	(103)	(29)	(6)	(203)	(164)	–	(733)
Goodwill impairment	–	–	–	–	(10,564)	–	–	(10,564)
Total operating expenses	(16,072)	(3,943)	(4,704)	(959)	(19,923)	(5,990)	2,492	(49,099)
Operating profit/(loss)	10,853	5,446	3,425	1,430	(15,539)	2,031	–	7,646
Share of profit in associates and joint ventures	16	15	1,297	316	11	6	–	1,661
Profit/(loss) before tax	10,869	5,461	4,722	1,746	(15,528)	2,037	–	9,307
Tax income/(expense)	(2,199)	(899)	(928)	(245)	1,715	(253)	–	(2,809)
Profit/(loss) for the year	8,670	4,562	3,794	1,501	(13,813)	1,784	–	6,498

Other information about the profit/(loss) for the year

	Europe US$m	Hong Kong US$m	Rest of Asia-Pacific US$m	Middle East US$m	North America US$m	Latin America US$m	Intra-HSBC items US$m	Total US$m
2010								
Net operating income	**19,730**	**10,088**	**8,793**	**1,783**	**8,752**	**8,187**	**(3,125)**	**54,208**
External	**18,881**	**9,170**	**7,728**	**1,774**	**8,504**	**8,151**	**–**	**54,208**
Inter-segment	**849**	**918**	**1,065**	**9**	**248**	**36**	**(3,125)**	**–**
Profit/(loss) for the year includes the following significant non-cash items:								
Depreciation, amortisation and impairment	**1,071**	**404**	**243**	**49**	**471**	**458**	**–**	**2,696**
Loan impairment losses gross of recoveries and other credit risk provisions	**3,303**	**169**	**615**	**684**	**8,476**	**1,812**	**–**	**15,059**
Impairment of financial investments	**35**	**41**	**4**	**5**	**21**	**1**	**–**	**107**
2009								
Net operating income	17,976	8,967	7,107	1,260	641	6,498	(2,756)	39,693
External	16,734	8,352	6,056	1,283	767	6,501	–	39,693
Inter-segment	1,242	615	1,051	(23)	(126)	(3)	(2,756)	–
Profit/(loss) for the year includes the following significant non-cash items:								
Depreciation, amortisation and impairment	1,039	342	215	37	515	390	–	2,538
Loan impairment losses gross of recoveries and other credit risk provisions	5,833	534	1,028	1,361	15,757	2,865	–	27,378
Impairment of financial investments	137	129	50	4	38	–	–	358
2008								
Net operating income	26,925	9,389	8,129	2,389	4,384	8,021	(2,492)	56,745
External	25,887	8,205	7,010	2,386	5,236	8,021	–	56,745
Inter-segment	1,038	1,184	1,119	3	(852)	–	(2,492)	–
Profit/(loss) for the year includes the following significant non-cash items:								
Depreciation, amortisation and impairment	1,093	312	192	31	11,352	387	–	13,367
Loan impairment losses gross of recoveries and other credit risk provisions	4,050	803	960	309	16,892	2,757	–	25,771
Impairment of financial investments	278	535	–	–	229	–	–	1,042

Notes on the Financial Statements (continued)

13 – Segmental analysis / 14 – Analysis of financial assets and liabilities

Performance ratios

	Europe %	Hong Kong %	Rest of Asia-Pacific %	Middle East %	North America %	Latin America %	Total %
2010							
Share of HSBC's profit before tax	**22.6**	**29.9**	**31.0**	**4.7**	**2.4**	**9.4**	**100.0**
Cost efficiency ratio	**67.9**	**43.4**	**55.7**	**44.7**	**48.8**	**65.7**	**55.2**
2009							
Share of HSBC's profit/(loss) before tax	56.7	71.0	59.3	6.4	(109.3)	15.9	100.0
Cost efficiency ratio	59.4	41.7	55.6	38.6	51.5	59.6	52.0
2008							
Share of HSBC's profit/(loss) before tax	116.7	58.7	50.7	18.8	(166.8)	21.9	100.0
Cost efficiency ratio	52.4	38.8	52.4	35.9	94.1	57.0	60.1

Balance sheet information

	Europe US$m	Hong Kong US$m	Rest of Asia-Pacific US$m	Middle East US$m	North America US$m	Latin America US$m	Intra-HSBC items US$m	Total US$m
At 31 December 2010								
Loans and advances to customers (net)	**435,799**	**140,691**	**108,731**	**24,626**	**190,532**	**57,987**	**–**	**958,366**
Interests in associates and joint ventures	**186**	**207**	**15,035**	**1,661**	**104**	**5**	**–**	**17,198**
Total assets	**1,249,527**	**429,565**	**278,062**	**52,757**	**492,487**	**139,938**	**(187,647)**	**2,454,689**
Customer accounts	**491,563**	**297,484**	**158,155**	**33,511**	**158,486**	**88,526**	**–**	**1,227,725**
Total liabilities	**1,189,996**	**422,101**	**246,989**	**45,379**	**459,301**	**123,655**	**(187,647)**	**2,299,774**
Capital expenditure incurred[1]	**865**	**836**	**168**	**46**	**774**	**788**	**–**	**3,477**
At 31 December 2009								
Loans and advances to customers (net)	439,481	99,381	80,043	22,844	206,853	47,629	–	896,231
Interests in associates and joint ventures	147	157	11,083	1,573	42	9	–	13,011
Total assets	1,268,600	399,243	222,139	48,107	475,014	115,967	(164,618)	2,364,452
Customer accounts	495,019	275,441	133,999	32,529	149,157	72,889	–	1,159,034
Total liabilities	1,213,907	384,912	203,243	42,325	447,530	101,492	(164,618)	2,228,791
Capital expenditure incurred[1]	983	290	159	102	658	540	–	2,732
At 31 December 2008								
Loans and advances to customers (net)	426,191	100,220	80,661	27,295	256,214	42,287	–	932,868
Interests in associates and joint ventures	137	153	9,728	1,383	128	8	–	11,537
Total assets	1,392,049	414,484	225,573	50,952	596,302	102,946	(254,841)	2,527,465
Customer accounts	502,476	250,517	124,194	35,165	143,532	59,443	–	1,115,327
Total liabilities	1,361,960	400,637	210,478	45,416	571,657	91,929	(254,841)	2,427,236
Capital expenditure incurred[1]	2,078	440	426	85	726	617	–	4,372

1 *Expenditure incurred on property, plant and equipment and other intangible assets. Excludes assets acquired as part of business combinations and goodwill.*

Other financial information

Net operating income by customer group and global business

	Personal Financial Services US$m	Commercial Banking US$m	Global Banking & Markets US$m	Global Private Banking US$m	Other[1] US$m	Intra-HSBC items US$m	Total US$m
2010							
Net operating income	**21,317**	**12,029**	**18,957**	**3,105**	**4,663**	**(5,863)**	**54,208**
External	**19,529**	**11,419**	**22,090**	**2,194**	**(1,024)**	**–**	**54,208**
Internal	**1,788**	**610**	**(3,133)**	**911**	**5,687**	**(5,863)**	**–**
2009							
Net operating income	15,513	9,571	18,652	2,984	(2,031)	(4,996)	39,693
External	13,804	9,285	21,383	2,275	(7,054)	–	39,693
Internal	1,709	286	(2,731)	709	5,023	(4,996)	–
2008							
Net operating income	20,269	13,144	12,047	3,563	12,290	(4,568)	56,745
External	15,023	13,080	17,739	2,231	8,672	–	56,745
Internal	5,246	64	(5,692)	1,332	3,618	(4,568)	–

1 *The main items reported in the 'Other' category are certain property activities, unallocated investment activities, centrally held investment companies, movements in fair value of own debt and HSBC's holding company and financing operations. The 'Other' category also includes gains and losses on the disposal of certain significant subsidiaries or business units.*

Information by country

	2010		2009		2008	
	External net operating income[1] US$m	**Non-current assets[2] US$m**	External net operating income[1] US$m	Non-current assets[2] US$m	External net operating income[1] US$m	Non-current assets[2] US$m
UK	**11,467**	**19,661**	9,958	19,704	15,789	12,491
Hong Kong	**9,170**	**4,630**	8,352	3,374	8,205	3,527
USA	**6,098**	**6,669**	(1,042)	5,499	2,862	4,660
France	**3,185**	**10,914**	3,322	11,782	6,457	11,862
Brazil	**4,506**	**2,025**	3,368	1,868	3,886	1,421
Other countries	**19,782**	**29,747**	15,735	25,557	19,546	23,020
	54,208	**73,646**	39,693	67,784	56,745	56,981

1 *External net operating income is attributed to countries on the basis of the location of the branch responsible for reporting the results or advancing the funds.*
2 *Non-current assets consist of property, plant and equipment, goodwill, other intangible assets, interests in associates and joint ventures and certain other assets expected to be recovered more than twelve months after the reporting period.*

14 Analysis of financial assets and liabilities by measurement basis

Financial assets and financial liabilities are measured on an ongoing basis either at fair value or at amortised cost. The summary of significant accounting policies in Note 2 describes how the classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the carrying amounts of the financial assets and liabilities by category as defined in IAS 39 and by balance sheet heading.

Notes on the Financial Statements (continued)

14 – Analysis of financial assets and liabilities

	At 31 December 2010							
	Held for trading US$m	Designated at fair value US$m	Held-to-maturity securities US$m	Available-for-sale securities US$m	Financial assets and liabilities at amortised cost US$m	Derivatives designated as fair value hedging instruments US$m	Derivatives designated as cash flow hedging instruments US$m	Total US$m
Financial assets								
Cash and balances at central banks	–	–	–	–	57,383	–	–	57,383
Items in the course of collection from other banks	–	–	–	–	6,072	–	–	6,072
Hong Kong Government certificates of indebtedness	–	–	–	–	19,057	–	–	19,057
Trading assets	385,052	–	–	–	–	–	–	385,052
Financial assets designated at fair value	–	37,011	–	–	–	–	–	37,011
Derivatives	256,689	–	–	–	–	596	3,472	260,757
Loans and advances to banks	–	–	–	–	208,271	–	–	208,271
Loans and advances to customers	–	–	–	–	958,366	–	–	958,366
Financial investments	–	–	19,499	381,256	–	–	–	400,755
Other assets	–	–	–	–	20,097	–	–	20,097
Accrued income	–	–	–	–	10,274	–	–	10,274
Total financial assets	641,741	37,011	19,499	381,256	1,279,520	596	3,472	2,363,095
Financial liabilities								
Hong Kong currency notes in circulation	–	–	–	–	19,057	–	–	19,057
Deposits by banks	–	–	–	–	110,584	–	–	110,584
Customer accounts	–	–	–	–	1,227,725	–	–	1,227,725
Items in the course of transmission to other banks	–	–	–	–	6,663	–	–	6,663
Trading liabilities	300,703	–	–	–	–	–	–	300,703
Financial liabilities designated at fair value	–	88,133	–	–	–	–	–	88,133
Derivatives	254,416	–	–	–	–	2,226	2,023	258,665
Debt securities in issue	–	–	–	–	145,401	–	–	145,401
Other liabilities	–	–	–	–	25,533	–	–	25,533
Accruals	–	–	–	–	12,545	–	–	12,545
Subordinated liabilities	–	–	–	–	33,387	–	–	33,387
Total financial liabilities	555,119	88,133	–	–	1,580,895	2,226	2,023	2,228,396

	At 31 December 2009							
	Held for trading US$m	Designated at fair value US$m	Held-to-maturity securities US$m	Available-for-sale securities US$m	Financial assets and liabilities at amortised cost US$m	Derivatives designated as fair value hedging instruments US$m	Derivatives designated as cash flow hedging instruments US$m	Total US$m
Financial assets								
Cash and balances at central banks	–	–	–	–	60,655	–	–	60,655
Items in the course of collection from other banks	–	–	–	–	6,395	–	–	6,395
Hong Kong Government certificates of indebtedness	–		–	–	17,463	–	–	17,463
Trading assets	421,381	–	–	–	–	–	–	421,381
Financial assets designated at fair value	–	37,181	–	–	–	–	–	37,181
Derivatives	245,685	–	–	–	–	584	4,617	250,886
Loans and advances to banks	–	–	–	–	179,781	–	–	179,781
Loans and advances to customers	–	–	–	–	896,231	–	–	896,231
Financial investments	–	–	17,626	351,532	–	–	–	369,158
Other assets	–	–	–	3	26,114	–	–	26,117
Accrued income	–	–	–	–	10,256	–	–	10,256
Total financial assets	667,066	37,181	17,626	351,535	1,196,895	584	4,617	2,275,504
Financial liabilities								
Hong Kong currency notes in circulation	–	–	–	–	17,463	–	–	17,463
Deposits by banks	–	–	–	–	124,872	–	–	124,872
Customer accounts	–	–	–	–	1,159,034	–	–	1,159,034
Items in the course of transmission to other banks	–	–	–	–	5,734	–	–	5,734
Trading liabilities	268,130	–	–	–	–	–	–	268,130
Financial liabilities designated at fair value	–	80,092	–	–	–	–	–	80,092
Derivatives	244,072	–	–	–	–	1,085	2,489	247,646
Debt securities in issue	–	–	–	–	146,896	–	–	146,896
Other liabilities	–	–	–	–	66,169	–	–	66,169
Accruals	–	–	–	–	11,644	–	–	11,644
Subordinated liabilities	–	–	–	–	30,478	–	–	30,478
Total financial liabilities	512,202	80,092	–	–	1,562,290	1,085	2,489	2,158,158

Notes on the Financial Statements (continued)

HSBC Holdings

	At 31 December 2010					
	Held for trading US$m	Designated at fair value US$m	Loans and receivables US$m	Available-for-sale securities US$m	Financial assets and liabilities at amortised cost US$m	Total US$m
Financial assets						
Cash at bank and in hand	–	–	–	–	459	459
Derivatives	2,327	–	–	–	–	2,327
Loans and advances to HSBC undertakings	–	–	21,238	–	–	21,238
Financial investments	–	–	–	2,025	–	2,025
Other assets	–	–	–	–	1	1
Total financial assets	2,327	–	21,238	2,025	460	26,050
Financial liabilities						
Amounts owed to HSBC undertakings	–	–	–	–	2,932	2,932
Financial liabilities designated at fair value	–	16,288	–	–	–	16,288
Derivatives	827	–	–	–	–	827
Debt securities in issue	–	–	–	–	2,668	2,668
Other liabilities	–	–	–	–	1,216	1,216
Accruals	–	–	–	–	566	566
Subordinated liabilities	–	–	–	–	13,313	13,313
Total financial liabilities	827	16,288	–	–	20,695	37,810

	At 31 December 2009					
	Held for trading US$m	Designated at fair value US$m	Loans and receivables US$m	Available-for-sale securities US$m	Financial assets and liabilities at amortised cost US$m	Total US$m
Financial assets						
Cash at bank and in hand	–	–	–	–	224	224
Derivatives	2,981	–	–	–	–	2,981
Loans and advances to HSBC undertakings	–	–	23,212	–	–	23,212
Financial investments	–	–	–	2,455	–	2,455
Other assets	–	–	–	–	4	4
Total financial assets	2,981	–	23,212	2,455	228	28,876
Financial liabilities						
Amounts owed to HSBC undertakings	–	–	–	–	3,711	3,711
Financial liabilities designated at fair value	–	16,909	–	–	–	16,909
Derivatives	362	–	–	–	–	362
Debt securities in issue	–	–	–	–	2,839	2,839
Other liabilities	–	–	–	–	8	8
Accruals	–	–	–	–	419	419
Subordinated liabilities	–	–	–	–	14,406	14,406
Total financial liabilities	362	16,909	–	–	21,383	38,654

15 Trading assets

	2010 US$m	2009 US$m
Trading assets:		
– not subject to repledge or resale by counterparties	**284,940**	320,155
– which may be repledged or resold by counterparties	**100,112**	101,226
	385,052	421,381
Treasury and other eligible bills	**25,620**	22,346
Debt securities	**168,268**	201,598
Equity securities	**41,086**	35,311
Trading securities at fair value	**234,974**	259,255
Loans and advances to banks	**70,456**	78,126
Loans and advances to customers	**79,622**	84,000
	385,052	421,381

Trading securities valued at fair value

	Fair value[1] 2010 US$m	Fair value[1] 2009 US$m
US Treasury and US Government agencies[2]	**20,239**	17,620
UK Government	**17,036**	12,113
Hong Kong Government	**11,053**	10,649
Other government	**92,826**	94,264
Asset-backed securities[3]	**3,998**	5,308
Corporate debt and other securities	**48,736**	83,990
Equity securities	**41,086**	35,311
	234,974	259,255

1 *Included within these figures are debt securities issued by banks and other financial institutions of US$37,170m (2009: US$41,466m), of which US$8,330m (2009: US$7,280m) are guaranteed by various governments.*
2 *Includes securities that are supported by an explicit guarantee issued by the US Government.*
3 *Excludes asset-backed securities included under US Treasury and US Government agencies.*

Trading securities listed on a recognised exchange and unlisted

	Treasury and other eligible bills US$m	Debt securities US$m	Equity securities US$m	Total US$m
Fair value at 31 December 2010				
Listed on a recognised exchange[1]	**698**	**113,878**	**40,098**	**154,674**
Unlisted	**24,922**	**54,390**	**988**	**80,300**
	25,620	**168,268**	**41,086**	**234,974**
Fair value at 31 December 2009				
Listed on a recognised exchange[1]	3,107	159,030	33,428	195,565
Unlisted	19,239	42,568	1,883	63,690
	22,346	201,598	35,311	259,255

1 *Included within listed investments are US$3,254m (2009: US$3,229m) of investments listed in Hong Kong.*

Loans and advances to banks held for trading

	2010 US$m	2009 US$m
Reverse repos	**45,771**	50,357
Settlement accounts	**5,226**	10,128
Stock borrowing	**6,346**	4,711
Other	**13,113**	12,930
	70,456	78,126

Loans and advances to customers held for trading

	2010 US$m	2009 US$m
Reverse repos	**46,366**	42,172
Settlement accounts	**7,516**	12,134
Stock borrowing	**11,161**	18,042
Other	**14,579**	11,652
	79,622	84,000

16 Fair values of financial instruments carried at fair value

The classification of financial instruments is determined in accordance with the accounting policies set out in Note 2. The use of assumptions and estimation in valuing financial instruments is described on page 34.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

The following table sets out the financial instruments carried at fair value.

Financial instruments carried at fair value and bases of valuation

		Valuation techniques		
	Quoted market price Level 1 US$m	Using observable inputs Level 2 US$m	With significant unobservable inputs Level 3 US$m	Total US$m
31 December 2010				
Assets				
Trading assets	**224,613**	**154,750**	**5,689**	**385,052**
Financial assets designated at fair value	**23,641**	**12,783**	**587**	**37,011**
Derivatives	**2,078**	**254,718**	**3,961**	**260,757**
Financial investments: available for sale	**214,276**	**158,743**	**8,237**	**381,256**
Liabilities				
Trading liabilities	**124,874**	**164,436**	**11,393**	**300,703**
Financial liabilities designated at fair value	**22,193**	**65,370**	**570**	**88,133**
Derivatives	**1,808**	**253,051**	**3,806**	**258,665**
31 December 2009				
Assets				
Trading assets	272,509	142,452	6,420	421,381
Financial assets designated at fair value	24,184	11,773	1,224	37,181
Derivatives	1,961	244,472	4,453	250,886
Financial investments: available for sale	163,149	178,168	10,214	351,531
Liabilities				
Trading liabilities	119,544	139,812	8,774	268,130
Financial liabilities designated at fair value	27,553	52,032	507	80,092
Derivatives	1,843	240,611	5,192	247,646

The reduction of Level 1 trading assets reflects the deconsolidation of CNAV funds which is discussed further on page 363. The increase in Level 1 available-for-sale instruments reflects increased investment in government and US agency securities. The rise in the size of Level 2 trading assets and liabilities reflects an increase in repo and reverse repo activity.

There were no material transfers between Level 1 and Level 2 in the period.

Control framework

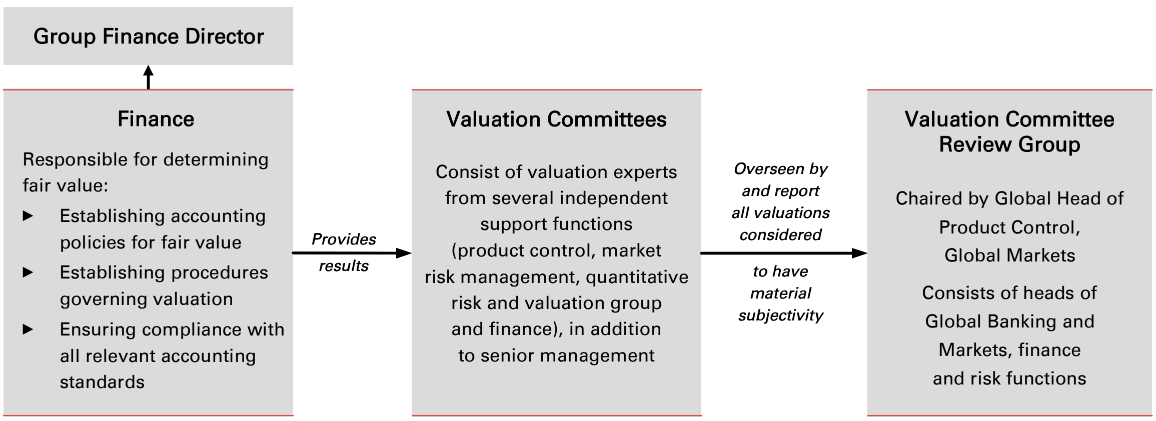
Fair values are subject to a control framework designed to ensure that they are either determined or validated by a function independent of the risk-taker.

For all financial instruments where fair values are determined by reference to externally quoted prices or observable pricing inputs to models, independent price determination or validation is utilised. In inactive markets, direct observation of a traded price may not be possible. In these circumstances, HSBC will source alternative market information to validate the financial instrument's fair value, with greater weight given to information that is considered to be more relevant and reliable. The factors that are considered in this regard are, *inter alia*:

- the extent to which prices may be expected to represent genuine traded or tradeable prices;
- the degree of similarity between financial instruments;
- the degree of consistency between different sources;
- the process followed by the pricing provider to derive the data;
- the elapsed time between the date to which the market data relates and the balance sheet date; and
- the manner in which the data was sourced.

For fair values determined using a valuation model, the control framework may include, as applicable, independent development or validation of (i) the logic within valuation models; (ii) the inputs to those models; (iii) any adjustments required outside the valuation models; and (iv) where possible, model outputs. Valuation models are subject to a process of due diligence and calibration before becoming operational and are calibrated against external market data on an ongoing basis.

The fair value governance structure is as follows:



Determination of fair value

Fair values are determined according to the following hierarchy:

- *Level 1 – quoted market price:* financial instruments with quoted prices for identical instruments in active markets.
- *Level 2 – valuation technique using observable inputs:* financial instruments with quoted prices for similar instruments in active markets or quoted prices for identical or similar instruments in inactive markets and financial instruments valued using models where all significant inputs are observable.
- *Level 3 – valuation technique with significant unobservable inputs:* financial instruments valued using valuation techniques where one or more significant inputs are unobservable.

The best evidence of fair value is a quoted price in an actively traded market. The fair values of financial instruments that are quoted in active markets are based on bid prices for assets held and offer prices for liabilities issued. Where a financial instrument has a quoted price in an active market and it is part of a portfolio, the fair value of the portfolio is calculated as the product of the number of units and quoted price and no block discounts are applied. In the event that the market for a financial instrument is not active, a valuation technique is used.

The judgement as to whether a market is active may include, but is not restricted to, the consideration of factors such as the magnitude and frequency of trading activity, the availability of prices and the size of bid/offer spreads. The bid/offer spread represents the difference in prices at which a market participant would be willing to buy compared with the price at which they would be willing to sell. In inactive markets, obtaining assurance that the transaction price provides evidence of fair value or determining the adjustments to transaction prices that are necessary to measure the fair value of the instrument requires additional work during the valuation process.

Valuation techniques incorporate assumptions about factors that other market participants would use in their valuations, including interest rate yield curves, exchange rates, volatilities, and prepayment and default rates. During the year, as a result of evolving market practice in the pricing of certain interest rate derivatives, HSBC has, for single currency swaps with collateralised counterparties and in significant major currencies, adopted a discounting curve that reflects the overnight interest rate ('OIS discounting'). Previously, in line with market practice, discount curves did not reflect this overnight interest rate component but were based on a term LIBOR rate. The financial effect of this change was not significant.

The majority of valuation techniques employ only observable market data. However, certain financial instruments are valued on the basis of valuation techniques that feature one or more significant market inputs that are unobservable, and for them, the derivation of fair value is more judgemental. An instrument in its entirety is classified as valued using significant unobservable inputs if, in the opinion of management, a significant proportion of the instrument's carrying amount and/or inception profit ('day 1 gain or loss') is driven by unobservable inputs. 'Unobservable' in this context means that there is little or no current market data available from which to determine the price at which an arm's length transaction would be likely to occur. It generally does not mean that there is no data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used).

In certain circumstances, primarily where debt is hedged with interest rate derivatives, HSBC records its own debt in issue at fair value, based on quoted prices in an active market for the specific instrument concerned, if available. When quoted market prices are unavailable, the own debt in issue is valued using valuation techniques, the inputs for which are either based upon quoted prices in an inactive market for the instrument, or are estimated by comparison with quoted prices in an active market for similar instruments. In both cases, the fair value includes the effect of applying the credit spread which is appropriate to HSBC's liabilities. The change in fair value of issued debt securities attributable to the Group's own credit spread is computed as follows: for each security at each reporting date, an externally verifiable price is obtained or a price is derived using credit spreads for similar securities for the same issuer. Then, using discounted cash flow, each security is valued using a LIBOR-based discount curve. The difference in the valuations is attributable to the Group's own credit spread. This methodology is applied consistently across all securities.

Structured notes issued and certain other hybrid instrument liabilities are included within trading liabilities and are measured at fair value. The credit spread applied to these instruments is derived from the spreads at which HSBC issues structured notes. These market spreads are smaller than credit spreads observed for plain vanilla debt or in the credit default swap markets.

Gains and losses arising from changes in the credit spread of liabilities issued by HSBC reverse over the contractual life of the debt, provided that the debt is not repaid at a premium or a discount.

Fair value adjustments

Fair value adjustments are adopted when HSBC considers that there are additional factors that would be considered by a market participant that are not incorporated within the valuation model. The magnitude of fair value adjustments depends upon many entity-specific factors, and therefore fair value adjustments may not be comparable across the banking industry.

HSBC classifies fair value adjustments as either 'risk-related' or 'model-related'. The majority of these adjustments relate to Global Banking and Markets.

Movements in the level of fair value adjustments do not necessarily result in the recognition of profits or losses within the income statement. For example, as models are enhanced, fair value adjustments may no longer be required. Similarly, fair value adjustments will decrease when the related positions are unwound, but this may not result in profit or loss.

Global Banking and Markets fair value adjustments

	At 31 December	
	2010	2009
	US$m	US$m
Type of adjustment		
Risk-related	**2,171**	2,955
Bid-offer	**620**	528
Uncertainty	**136**	223
Credit risk adjustment	**1,355**	2,172
Other	**60**	32
Model-related	**389**	457
Model limitation	**383**	391
Other	**6**	66
Inception profit (Day 1 P&L reserves) (Note 20)	**250**	260
	2,810	3,672

The most significant fair value adjustment movement related to the release of US$490m of credit risk adjustments held for monoline insurers of which US$336m resulted from commutations. The commutations did not result in a material gain or loss. The remainder of the decrease in the credit risk adjustment derived primarily from commutations or restructures with non-monoline counterparties and internal credit rating upgrades of certain counterparties.

Risk-related adjustments

Bid-offer

IAS 39 requires that portfolios are marked at bid or offer, as appropriate. Valuation models will typically generate mid market values. The bid-offer adjustment reflects the cost that would be incurred if substantially all residual net portfolio market risks were closed using available hedging instruments or by disposing of or unwinding the actual position.

Uncertainty

Certain model inputs may be less readily determinable from market data, and/or the choice of model itself may be more subjective. In these circumstances, there exists a range of possible values that the financial instrument or market parameter may assume and an adjustment may be necessary to reflect the likelihood that in estimating the fair value of the financial instrument, market participants would adopt rather more conservative values for uncertain parameters and/or model assumptions than those used in the valuation model.

Credit risk adjustment

The credit risk adjustment is an adjustment to the valuation of OTC derivative contracts to reflect within fair value the possibility that the counterparty may default and HSBC may not receive the full market value of the transactions.

Model-related adjustments

Model limitation

Models used for portfolio valuation purposes may be based upon a simplifying set of assumptions that do not capture all material market characteristics. Additionally, markets evolve, and models that were adequate in the past may require development to capture all material market characteristics in current market conditions. In these circumstances, model limitation adjustments are adopted. As model development progresses, model limitations are addressed within the valuation models and a model limitation adjustment is no longer needed.

Inception profit (Day 1 P&L reserves)

Inception profit adjustments are adopted where the fair value estimated by a valuation model is based on one or more significant unobservable inputs. The accounting for inception profit adjustments is discussed on page 254. An analysis of the movement in the deferred Day 1 P&L reserve is provided on page 324.

Notes on the Financial Statements (continued)

Credit risk adjustment methodology

HSBC calculates a separate credit risk adjustment for each HSBC legal entity, and within each entity for each counterparty to which the entity has exposure. The calculation of the monoline credit risk adjustment and sensitivity to different assumptions is described on page 137. Of the total credit risk adjustment at 31 December 2010 of US$1,355m (2009: US$2,172m), US$836m (2009: US$1,163m) relates to the credit risk adjustment taken against non-monoline counterparties. The methodology for calculating the credit risk adjustment for non-monoline counterparties is described below.

HSBC calculates the credit risk adjustment by applying the probability of default of the counterparty to the expected positive exposure to the counterparty, and multiplying the result by the loss expected in the event of default. The calculation is performed over the life of the potential exposure.

The probability of default is based on HSBC's internal credit rating for the counterparty, taking into account how credit ratings may deteriorate over the duration of the exposure through the use of historical rating transition matrices. For most products, to calculate the expected positive exposure to a counterparty, HSBC uses a simulation methodology to incorporate the range of potential exposures across the portfolio of transactions with the counterparty over the life of an instrument. The simulation methodology includes credit mitigants such as counterparty netting agreements and collateral agreements with the counterparty. A standard loss given default assumption of 60% is generally adopted. HSBC does not adjust derivative liabilities for HSBC's own credit risk, such an adjustment is often referred to as a 'debit valuation adjustment'.

For certain types of exotic derivatives where the products are not currently supported by the simulation, or for derivative exposures in smaller trading locations where the simulation tool is not yet available, HSBC adopts alternative methodologies. These may involve mapping to the results for similar products from the simulation tool or where such a mapping approach is not appropriate, a simplified methodology is used, generally following the same principles as the simulation methodology. The calculation is applied at a trade level, with more limited recognition of credit mitigants such as netting or collateral agreements than used in the simulation methodology described previously.

The methodologies do not, in general, account for 'wrong-way risk'. Wrong-way risk arises where the underlying value of the derivative prior to any credit risk adjustment is positively correlated to the probability of default of the counterparty. Where there is significant wrong-way risk, a trade specific approach is applied to reflect the wrong-way risk within the valuation.

HSBC includes all third party counterparties in the credit risk adjustment calculation and does not net credit risk adjustments across HSBC Group entities. During 2010, there were no material changes made by HSBC to the methodologies used to calculate the credit risk adjustment.

Fair value valuation bases

Financial instruments measured at fair value using a valuation technique with significant unobservable inputs – Level 3

	Assets				Liabilities		
	Available for sale US$m	Held for trading US$m	Designated at fair value through profit or loss US$m	Derivatives US$m	Held for trading US$m	Designated at fair value through profit or loss US$m	Derivatives US$m
At 31 December 2010							
Private equity including strategic investments	4,057	278	120	–	–	–	–
Asset-backed securities	1,949	566	–	–	–	–	–
Leveraged finance	–	–	–	–	–	–	11
Loans held for securitisation	–	1,043	–	–	–	–	–
Structured notes	–	–	–	–	10,667	–	–
Derivatives with monolines	–	–	–	1,005	–	–	–
Other derivatives	–	–	–	2,956	–	–	3,787
Other portfolios	2,231	3,802	467	–	726	570	8
	8,237	5,689	587	3,961	11,393	570	3,806

	Assets				Liabilities		
	Available for sale US$m	Held for trading US$m	Designated at fair value through profit or loss US$m	Derivatives US$m	Held for trading US$m	Designated at fair value through profit or loss US$m	Derivatives US$m
At 31 December 2009							
Private equity and strategic investments	2,949	197	345	–	–	–	–
Asset-backed securities	4,270	944	–	–	–	–	–
Leveraged finance	–	73	–	–	–	–	25
Loans held for securitisation	–	1,395	–	–	–	–	–
Structured notes	–	196	–	–	5,055	–	–
Derivatives with monolines	–	–	–	1,305	–	–	–
Other derivatives	–	–	–	3,148	–	–	5,167
Other portfolios	2,995	3,615	879	–	3,719	507	–
	10,214	6,420	1,224	4,453	8,774	507	5,192

Private equity and strategic investments

HSBC's private equity and strategic investments are generally classified as available for sale and are not traded in active markets. In the absence of an active market, an investment's fair value is estimated on the basis of an analysis of the investee's financial position and results, risk profile, prospects and other factors, as well as by reference to market valuations for similar entities quoted in an active market, or the price at which similar companies have changed ownership.

Asset-backed securities

Illiquidity and a lack of transparency in the market for ABSs have resulted in less observable data being available. While quoted market prices are generally used to determine the fair value of these securities, valuation models are used to substantiate the reliability of the limited market data available and to identify whether any adjustments to quoted market prices are required. For ABSs including residential MBSs, the valuation uses an industry standard model and the assumptions relating to prepayment speeds, default rates and loss severity based on collateral type, and performance, as appropriate. The valuations output is benchmarked for consistency against observable data for securities of a similar nature.

Loans, including leveraged finance and loans held for securitisation

Loans held at fair value are valued from broker quotes and/or market data consensus providers when available. In the absence of an observable market, the fair value is determined using valuation techniques. These techniques include discounted cash flow models, which incorporate assumptions regarding an appropriate credit spread for the loan, derived from other market instruments issued by the same or comparable entities.

Structured notes

The fair value of structured notes valued using a valuation technique is derived from the fair value of the underlying debt security, and the fair value of the embedded derivative is determined as described in the paragraph below on derivatives.

Derivatives

OTC (i.e. non-exchange traded) derivatives are valued using valuation models. Valuation models calculate the present value of expected future cash flows, based upon 'no-arbitrage' principles. For many vanilla derivative products, such as interest rate swaps and European options, the modelling approaches used are standard across the industry. For more complex derivative products, there may be some differences in market practice. Inputs to valuation models are determined from observable market data wherever possible, including prices available from exchanges, dealers, brokers or providers of consensus pricing. Certain inputs may not be observable in the market directly, but can be determined from observable prices via model calibration procedures or estimated from historical data or other sources. Examples of inputs that may be unobservable include volatility surfaces, in whole or in part, for less commonly traded option products, and correlations between market factors such as foreign exchange rates, interest rates and equity prices. The valuation of derivatives with monolines is discussed on page 137.

Notes on the Financial Statements (continued)

16 – Fair values of financial instruments carried at fair value

Reconciliation of fair value measurements in Level 3 of the fair value hierarchy

The following table provides a reconciliation of the movement between opening and closing balances of Level 3 financial instruments, measured at fair value using a valuation technique with significant unobservable inputs:

Movement in Level 3 financial instruments

	Assets				Liabilities		
	Available for sale US$m	Held for trading US$m	Designated at fair value through profit or loss US$m	Derivatives US$m	Held for trading US$m	Designated at fair value through profit or loss US$m	Derivatives US$m
2010							
At 1 January	**10,214**	**6,420**	**1,224**	**4,453**	**8,774**	**507**	**5,192**
Total gains/(losses) recognised in profit or loss	**345**	**158**	**63**	**(675)**	**166**	**(11)**	**(240)**
Total gains/(losses) recognised in other comprehensive income[1]	**618**	**(101)**	**(36)**	**(110)**	**(157)**	**74**	**93**
Purchases	**3,708**	**858**	**81**	**–**	**(356)**	**–**	**–**
New issuances	**–**	**–**	**–**	**–**	**4,025**	**–**	**–**
Sales	**(2,461)**	**(1,543)**	**(8)**	**–**	**–**	**–**	**–**
Settlements	**(1,032)**	**1**	**(22)**	**64**	**(948)**	**–**	**(820)**
Transfers out	**(7,065)**	**(629)**	**(894)**	**(669)**	**(1,750)**	**–**	**(1,003)**
Transfers in	**3,910**	**525**	**179**	**898**	**1,639**	**–**	**584**
At 31 December	**8,237**	**5,689**	**587**	**3,961**	**11,393**	**570**	**3,806**
Total gains/(losses) recognised in profit or loss relating to assets and liabilities held on 31 December:	**113**	**116**	**17**	**268**	**180**	**(14)**	**361**
– net interest income	**89**	**–**	**–**	**–**	**–**	**–**	**–**
– trading income excluding net interest income	**–**	**98**	**–**	**268**	**198**	**–**	**361**
– net interest income on trading activities	**–**	**18**	**–**	**–**	**(18)**	**–**	**–**
– net income/(expense) from other financial instruments designated at fair value	**–**	**–**	**17**	**–**	**–**	**(14)**	**–**
– dividend income	**24**	**–**	**–**	**–**	**–**	**–**	**–**
2009							
At 1 January	9,116	7,561	460	9,883	6,509	–	3,805
Total gains/(losses) recognised in profit or loss	(260)	(730)	97	(5,275)	(107)	(3)	(1,372)
Total gains recognised in other comprehensive income[1]	617	85	–	119	301	10	94
Purchases	1,785	1,598	260	–	22	–	–
New issuances	–	–	–	–	2,522	500	–
Sales	(806)	(2,166)	(13)	–	–	–	–
Settlements	(1,059)	(295)	(6)	(104)	(1,266)	–	(206)
Transfers out	(3,043)	(1,077)	–	(1,057)	(537)	–	(620)
Transfers in	3,864	1,444	426	887	1,330	–	3,491
At 31 December	10,214	6,420	1,224	4,453	8,774	507	5,192
Total gains/(losses) recognised in profit or loss relating to assets and liabilities held on 31 December:	(371)	(596)	98	(3,753)	(136)	(3)	(135)
– net interest income	(364)	–	–	–	–	–	–
– trading income excluding net interest income	–	(640)	98	(3,753)	(135)	–	(135)
– net interest income on trading activities	–	44	–	–	(1)	–	–
– gains less losses from financial investments	(9)	–	–	–	–	–	–
– net income/(expense) from other financial instruments designated at fair value	–	–	–	–	–	(3)	–
– dividend income	2	–	–	–	–	–	–

1 *Included in 'Available-for-sale investments: Fair value gains/(losses)' and 'Exchange differences' in the consolidated statement of comprehensive income.*

Available-for-sale securities: Greater pricing certainty of valuations in ABS markets (particularly MBS) has resulted in the transfer of assets out of Level 3 during 2010. Transfers into Level 3 were primarily related to strategic investments in Asia.

Trading assets: Greater pricing certainty of valuations in ABS markets (particularly MBS) and certain corporate bonds has resulted in the transfer of assets out of Level 3 during 2010. Transfers into Level 3 were driven by certain other corporate bonds for which pricing certainty decreased. Sales relate to disposals of whole loans, municipal bonds and various ABSs.

Derivative assets: Transfers out of Level 3 were driven by increased observability of longer-dated equity index volatility, particularly in Asian markets. Transfers in relate primarily to quanto structured credit transactions. Commutations of monoline derivatives and the narrowing of credit spreads have led to an overall reduction in the value of Level 3 assets.

Trading liabilities: Transfers out of and in to Level 3 relate primarily to increased / decreased observability of structured notes with embedded equity derivatives. New issuances relate to structured notes particularly those with embedded equity derivatives issued in the US.

Derivative liabilities: The increased observability in certain OTC equity derivative markets primarily in Asia led to transfers out of Level 3. Transfers in were driven by structured credit transactions.

Effect of changes in significant unobservable assumptions to reasonably possible alternatives

As discussed above, the fair value of financial instruments are, in certain circumstances, measured using valuation techniques that incorporate assumptions that are not evidenced by prices from observable current market transactions in the same instrument and are not based on observable market data. The following table shows the sensitivity of these fair values to reasonably possible alternative assumptions:

Sensitivity of fair values to reasonably possible alternative assumptions

	Reflected in profit or loss		Reflected in other comprehensive income	
	Favourable changes US$m	Unfavourable changes US$m	Favourable changes US$m	Unfavourable changes US$m
At 31 December 2010				
Derivatives, trading assets and trading liabilities[1]	**554**	**(444)**	**–**	**–**
Financial assets and liabilities designated at fair value	**77**	**(75)**	**–**	**–**
Financial investments: available for sale	**–**	**–**	**763**	**(744)**
	631	**(519)**	**763**	**(744)**
At 31 December 2009				
Derivatives, trading assets and trading liabilities[1]	984	(577)	–	–
Financial assets and liabilities designated at fair value	102	(98)	–	–
Financial investments: available for sale	–	–	1,161	(1,157)
	1,086	(675)	1,161	(1,157)

1 *Derivatives, trading assets and trading liabilities are presented as one category to reflect the manner in which these financial instruments are risk-managed.*

The decrease in the effect of changes in significant unobservable inputs in relation to derivatives, trading assets and trading liabilities during the year primarily reflected the decreased sensitivity to monoline credit risk adjustment assumptions as exposures have reduced. The decrease in the effect of changes in significant unobservable inputs for available-for-sale assets arose from increased pricing certainty in respect of ABSs.

Notes on the Financial Statements (continued)

16 – Fair values of financial instruments carried at fair value

Sensitivity of fair values to reasonably possible alternative assumptions by Level 3 instrument type

	Reflected in profit or loss		Reflected in other comprehensive income	
	Favourable changes US$m	Unfavourable changes US$m	Favourable changes US$m	Unfavourable changes US$m
At 31 December 2010				
Private equity investments	**112**	**(71)**	**383**	**(383)**
Asset-backed securities	**8**	**(8)**	**179**	**(181)**
Loans held for securitisation	**8**	**(8)**	**–**	**–**
Structured notes	**18**	**(16)**	**–**	**–**
Derivatives with monolines	**94**	**(8)**	**–**	**–**
Other derivatives	**256**	**(258)**	**–**	**–**
Other portfolios	**135**	**(150)**	**201**	**(180)**
	631	**(519)**	**763**	**(744)**
At 31 December 2009				
Private equity investments	54	(54)	302	(299)
Asset-backed securities	41	(41)	734	(735)
Leveraged finance	1	(1)	–	–
Loans held for securitisation	16	(16)	–	–
Structured notes	3	(3)	–	–
Derivatives with monolines	333	(25)	–	–
Other derivatives	309	(332)	–	–
Other portfolios	329	(203)	125	(123)
	1,086	(675)	1,161	(1,157)

Favourable and unfavourable changes are determined on the basis of changes in the value of the instrument as a result of varying the levels of the unobservable parameters using statistical techniques. When parameters are not amenable to statistical analysis, quantification of uncertainty is judgemental.

When the fair value of a financial instrument is affected by more than one unobservable assumption, the above table reflects the most favourable or most unfavourable change from varying the assumptions individually.

In respect of private equity investments, in many of the methodologies, the principal assumption is the valuation multiple to be applied to the main financial indicators. This may be determined with reference to multiples for comparable listed companies and includes discounts for marketability.

For ABSs, the principal assumptions in the models are based on benchmark information about prepayment speeds, default rates, loss severities and the historical performance of the underlying assets.

For leveraged finance, loans held for securitisation and derivatives with monolines the principal assumption concerns the appropriate value to be attributed to the counterparty credit risk. This requires estimation of exposure at default, probability of default and recovery in the event of default. For loan transactions, assessment of exposure at default is straightforward. For derivative transactions, a future exposure profile is generated on the basis of current market data. Probabilities of default and recovery levels are estimated using available evidence, which may include financial information, historical experience, CDS spreads and consensus recovery levels.

For structured notes and other derivatives, principal assumptions concern the value to be attributed to future volatility of asset values and the future correlation between asset values. These principal assumptions include credit volatilities and correlations used in the valuation of structured credit derivatives (including leveraged credit derivatives). For such unobservable assumptions, estimates are based on available market data, which may include the use of a proxy method to derive a volatility or a correlation from comparable assets for which market data is more readily available, and/or an examination of historical levels.

HSBC Holdings

The following table provides an analysis of the basis for valuing financial assets and financial liabilities measured at fair value in the financial statements:

Bases of valuing HSBC Holdings' financial assets and liabilities measured at fair value

	Valuation techniques			
	Quoted market price Level 1 US$m	Using observable inputs Level 2 US$m	With significant unobservable inputs Level 3 US$m	Total US$m
At 31 December 2010				
Assets				
Derivatives	**–**	**2,327**	**–**	**2,327**
Financial investments: available for sale	**–**	**–**	**2,025**	**2,025**
Liabilities				
Financial liabilities designated at fair value	**12,029**	**4,259**	**–**	**16,288**
Derivatives	**–**	**827**	**–**	**827**
At 31 December 2009				
Assets				
Derivatives	–	2,981	–	2,981
Financial investments: available for sale	–	–	2,455	2,455
Liabilities				
Financial liabilities designated at fair value	12,549	4,360	–	16,909
Derivatives	–	362	–	362

Financial instruments measured at fair value – Level 3

Financial investments measured using a valuation technique with significant unobservable inputs (Level 3) comprise fixed-rate preferred securities and senior notes purchased from HSBC undertakings. The unobservable elements of the valuation technique include the use of implied credit spreads and simplified bond pricing assumptions.

Movement in Level 3 financial instruments available for sale

	2010 US$m	2009 US$m
At 1 January	**2,455**	2,629
Total gains or losses:		
– recognised in profit or loss	**(155)**	(2)
– recognised in other comprehensive income	**(275)**	103
Settlements	**–**	(275)
At 31 December	**2,025**	2,455
Total gains or losses recognised in profit or loss relating to those assets and liabilities held on 31 December	**(1)**	(2)

In certain circumstances, the fair value of financial instruments are measured using valuation models that incorporate assumptions that are not supported by prices from observable current market transactions in the same instrument and are not based on observable market data. The following table shows the sensitivity of non-derivative financial instruments to reasonably possible alternative assumptions:

Effect of changes in significant unobservable assumptions to reasonably possible alternatives

	Reflected in equity	
	Favourable changes US$m	Unfavourable changes US$m
Financial investments: available for sale		
At 31 December 2010	**34**	**(33)**
At 31 December 2009	115	(107)

17 Fair values of financial instruments not carried at fair value

The classification of financial instruments is determined in accordance with the accounting policies set out in Note 2.

Fair values of financial instruments which are not carried at fair value on the balance sheet

	At 31 December 2010		At 31 December 2009	
	Carrying amount US$m	**Fair value US$m**	Carrying amount US$m	Fair value US$m
Assets				
Loans and advances to banks	**208,271**	**208,311**	179,781	179,658
Loans and advances to customers	**958,366**	**934,444**	896,231	855,780
Financial investments: debt securities	**19,386**	**20,374**	17,526	18,097
Financial investments: treasury and other eligible bills	**113**	**113**	101	101
Liabilities				
Deposits by banks	**110,584**	**110,563**	124,872	124,856
Customer accounts	**1,227,725**	**1,227,428**	1,159,034	1,160,036
Debt securities in issue	**145,401**	**145,417**	146,896	145,888
Subordinated liabilities	**33,387**	**33,161**	30,478	30,307

Fair values of financial instruments held for sale which are not carried at fair value on the balance sheet

	At 31 December 2010		At 31 December 2009	
	Carrying amount US$m	**Fair value US$m**	Carrying amount US$m	Fair value US$m
Assets classified as held for sale				
Loans and advances to banks and customers	**116**	**116**	1,356	1,316

The following is a list of financial instruments whose carrying amount is a reasonable approximation of fair value because, for example, they are short-term in nature or reprice to current market rates frequently:

Assets
Cash and balances at central banks
Items in the course of collection from other banks
Hong Kong Government certificates of indebtedness
Endorsements and acceptances
Short-term receivables within 'Other assets'
Accrued income

Liabilities
Hong Kong currency notes in circulation
Items in the course of transmission to other banks
Investment contracts with discretionary participation features within 'Liabilities under insurance contracts'
Endorsements and acceptances
Short-term payables within 'Other liabilities'
Accruals

Analysis of loans and advances to customers by geographical segment

	At 31 December 2010		At 31 December 2009	
	Carrying amount US$m	**Fair value US$m**	Carrying amount US$m	Fair value US$m
Loans and advances to customers				
Europe	**435,799**	**430,333**	439,481	431,158
Hong Kong	**140,691**	**140,699**	99,381	99,694
Rest of Asia-Pacific	**108,731**	**108,582**	80,043	79,972
Middle East	**24,626**	**24,539**	22,844	22,538
North America	**190,532**	**172,522**	206,853	174,957
Latin America	**57,987**	**57,769**	47,629	47,461
	958,366	**934,444**	896,231	855,780

Valuation

The calculation of fair value incorporates HSBC's estimate of the amount at which financial assets could be exchanged, or financial liabilities settled, between knowledgeable, willing parties in an arm's length transaction. It does not reflect the economic benefits and costs that HSBC expects to flow from the instruments' cash flows over their expected future lives. Other reporting entities may use different valuation methodologies and assumptions in determining fair values for which no observable market prices are available, so comparisons of fair values between entities may not be meaningful and users are advised to exercise caution when using this data.

Loans and advances to banks and customers

The fair value of loans and advances is based on observable market transactions, where available. In the absence of observable market transactions, fair value is estimated using discounted cash flow models.

Performing loans are grouped, as far as possible, into homogeneous pools segregated by maturity and interest rates and the contractual cash flows are generally discounted using HSBC's estimate of the discount rate that a market participant would use in valuing instruments with similar maturity, re-pricing and credit risk characteristics.

The fair value of a loan portfolio reflects both loan impairments at the balance sheet date and estimates of market participants' expectations of credit losses over the life of the loans. For impaired loans, fair value is estimated by discounting the future cash flows over the time period they are expected to be recovered.

Financial investments

The fair values of listed financial investments are determined using bid market prices. The fair values of unlisted financial investments are determined using valuation techniques that take into consideration the prices and future earnings streams of equivalent quoted securities.

Deposits by banks and customer accounts

For the purpose of estimating fair value, deposits by banks and customer accounts are grouped by remaining contractual maturity. Fair values are estimated using discounted cash flows, applying current rates offered for deposits of similar remaining maturities. The fair value of a deposit repayable on demand is assumed to be the amount payable on demand at the balance sheet date.

Debt securities in issue and subordinated liabilities

Fair values are determined using quoted market prices at the balance sheet date where available, or by reference to quoted market prices for similar instruments.

The fair values in this note are stated at a specific date and may be significantly different from the amounts which will actually be paid on the maturity or settlement dates of the instruments. In many cases, it would not be possible to realise immediately the estimated fair values given the size of the portfolios measured. Accordingly, these fair values do not represent the value of these financial instruments to HSBC as a going concern.

HSBC Holdings

The methods used by HSBC Holdings to determine fair values of financial instruments for the purpose of measurement and disclosure are described above.

The following table provides an analysis of the fair value of financial instruments not carried at fair value on the balance sheet:

Notes on the Financial Statements (continued)

Fair values of HSBC Holdings' financial instruments not carried at fair value on the balance sheet

	At 31 December 2010		At 31 December 2009	
	Carrying amount US$m	Fair value US$m	Carrying amount US$m	Fair value US$m
Assets				
Loans and advances to HSBC undertakings	21,238	21,798	23,212	23,871
Liabilities				
Amounts owed to HSBC undertakings	2,932	2,963	3,711	3,827
Debt securities in issue	2,668	2,960	2,839	3,141
Subordinated liabilities	13,313	14,428	14,406	15,666

18 Reclassification of financial assets

During the second half of 2008, HSBC reclassified US$15.3bn and US$2.6bn of financial assets from the held-for-trading category to the loans and receivables and available-for-sale classifications, respectively, as permitted by the relevant amendment to IAS 39 and explained in Note 2(e) on the Financial Statements. No further reclassifications were undertaken by HSBC in 2010 and 2009.

Reclassification of HSBC's financial assets

	At 31 December 2010		At 31 December 2009	
	Carrying amount US$m	Fair value US$m	Carrying amount US$m	Fair value US$m
Reclassification to loans and receivables				
ABSs	5,892	4,977	7,827	6,177
Trading loans – commercial mortgage loans	522	493	553	506
Leveraged finance and syndicated loans	4,533	4,166	5,824	5,434
	10,947	9,636	14,204	12,117
Reclassification to available for sale				
Corporate debt and other securities	91	91	1,408	1,408
	11,038	9,727	15,612	13,525

The following table shows the fair value gains and losses, income and expense recognised in the income statement in respect of reclassified assets and the gains and losses that would have been recognised if no reclassification had taken place.

Effect of reclassifying and not reclassifying financial assets

	Financial assets reclassified to:					
	loans and receivables				available for sale	
	ABSs US$m	Trading loans – commercial mortgage loans US$m	Leveraged finance and syndicated loans US$m	Total US$m	Corporate debt and other securities US$m	Total US$m
2010						
Recorded in the income statement[1]	235	29	346	610	56	666
Assuming no reclassification[2]	908	45	307	1,260	59	1,319
Net effect of reclassification	(673)	(16)	39	(650)	(3)	(653)
Attributable to:						
Europe	(527)	(16)	(23)	(566)	(2)	(568)
North America	(146)	–	49	(97)	(1)	(98)
Middle East	–	–	13	13	–	13

	Financial assets reclassified to:					
	loans and receivables				available for sale	
	ABSs US$m	Trading loans – commercial mortgage loans US$m	Leveraged finance and syndicated loans US$m	Total US$m	Corporate debt and other securities US$m	Total US$m
2009						
Recorded in the income statement[1]	511	32	434	977	101	1,078
Assuming no reclassification[2]	767	15	1,494	2,276	301	2,577
Net effect of reclassification	(256)	17	(1,060)	(1,299)	(200)	(1,499)
Attributable to:						
Europe	(212)	17	(566)	(761)	(170)	(931)
North America	(44)	–	(543)	(587)	(30)	(617)
Middle East	–	–	49	49	–	49
2008						
Recorded in the income statement[1]	303	17	192	512	22	534
Assuming no reclassification[2]	(1,549)	(13)	(1,239)	(2,801)	(202)	(3,003)
Net effect of reclassification	1,852	30	1,431	3,313	224	3,537
Attributable to:						
Europe	1,537	30	803	2,370	193	2,563
North America	315	–	601	916	31	947
Middle East	–	–	27	27	–	27

1 *'Income and expense' recorded in the income statement represents the accrual of the effective interest rate and, for 2010, includes US$6m in respect of impairment (2009: US$163m; 2008: US$26m). The effect on the income statement for 2008 shows the income and expense post-reclassification. In 2008 pre-reclassification, the assets were held at fair value and a loss of US$1,371m was recorded in the period up to reclassification.*
2 *Effect on the income statement during the year had the reclassification not occurred.*

19 Financial assets designated at fair value

	2010 US$m	2009 US$m
Financial assets designated at fair value:		
– not subject to repledge or resale by counterparties	**36,990**	37,166
– which may be repledged or resold by counterparties	**21**	15
	37,011	37,181
Treasury and other eligible bills	**159**	223
Debt securities	**18,248**	20,718
Equity securities	**17,418**	14,983
Securities designated at fair value	**35,825**	35,924
Loans and advances to banks	**315**	354
Loans and advances to customers	**871**	903
	37,011	37,181

Securities designated at fair value

	Fair value[1] 2010 US$m	2009 US$m
US Treasury and US Government agencies[2]	**78**	78
UK Government	**1,304**	4,799
Hong Kong Government	**151**	177
Other government	**4,130**	3,491
Asset-backed securities[3]	**6,128**	6,463
Corporate debt and other securities	**6,616**	5,933
Equities	**17,418**	14,983
	35,825	35,924

1 *Included within these figures are debt securities issued by banks and other financial institutions of US$10,185m (2009: US$13,745m), of which US$48m (2009: US$49m) are guaranteed by various governments.*
2 *Includes securities that are supported by an explicit guarantee issued by the US Government.*
3 *Excludes asset-backed securities included under US Treasury and US Government agencies.*

Securities listed on a recognised exchange and unlisted

	Treasury and other eligible bills US$m	Debt securities US$m	Equity securities US$m	Total US$m
Fair value at 31 December 2010				
Listed on a recognised exchange[1]	**21**	**4,168**	**12,548**	**16,737**
Unlisted	**138**	**14,080**	**4,870**	**19,088**
	159	**18,248**	**17,418**	**35,825**
Fair value at 31 December 2009				
Listed on a recognised exchange[1]	78	7,168	10,549	17,795
Unlisted	145	13,550	4,434	18,129
	223	20,718	14,983	35,924

1 *Included within listed investments are US$756m of investments listed in Hong Kong (2009: US$506m).*

20 Derivatives

Fair values of derivatives by product contract type held by HSBC

	Assets			Liabilities		
	Trading US$m	Hedging US$m	Total US$m	Trading US$m	Hedging US$m	Total US$m
At 31 December 2010						
Foreign exchange	**65,905**	**1,304**	**67,209**	**67,564**	**340**	**67,904**
Interest rate	**278,364**	**2,764**	**281,128**	**273,222**	**3,909**	**277,131**
Equity	**13,983**	**–**	**13,983**	**14,716**	**–**	**14,716**
Credit	**20,907**	**–**	**20,907**	**20,027**	**–**	**20,027**
Commodity and other	**1,261**	**–**	**1,261**	**2,618**	**–**	**2,618**
Gross total fair values	**380,420**	**4,068**	**384,488**	**378,147**	**4,249**	**382,396**
Netting			**(123,731)**			**(123,731)**
Total			**260,757**			**258,665**
At 31 December 2009						
Foreign exchange	55,036	1,695	56,731	54,502	300	54,802
Interest rate	212,102	3,506	215,608	209,351	3,274	212,625
Equity	15,729	–	15,729	19,013	–	19,013
Credit	28,479	–	28,479	27,042	–	27,042
Commodity and other	1,135	–	1,135	960	–	960
Gross total fair values	312,481	5,201	317,682	310,868	3,574	314,442
Netting			(66,796)			(66,796)
Total			250,886			247,646

The 4% increase in the fair value of derivative assets during 2010 was driven both by this increased volume of open trades and by small net declines in yield curves of major currencies over the year. The netting adjustment increased as increasing volumes of transactions, particularly interest rate derivatives and credit derivatives, were executed through clearing houses, where the settlement arrangements satisfied the IFRS netting criteria.

Fair values of derivatives by product contract type held by HSBC Holdings with subsidiaries

	At 31 December 2010		At 31 December 2009	
	Trading assets US$m	**Trading liabilities US$m**	Trading assets US$m	Trading liabilities US$m
Foreign exchange	**1,407**	**827**	2,250	362
Interest rate	**920**	**–**	731	–
	2,327	**827**	2,981	362

Derivatives are financial instruments that derive their value from the price of underlying items such as equities, bonds, interest rates, foreign exchange, credit spreads, commodities and equity or other indices. Derivatives enable users to increase, reduce or alter exposure to credit or market risks. HSBC makes markets in derivatives for its customers and uses derivatives to manage its exposure to credit and market risks.

Derivatives are carried at fair value and shown in the balance sheet as separate totals of assets and liabilities. A description of how the fair value of derivatives is derived is set out on page 313. Derivative assets and liabilities on different transactions are only set off if the transactions are with the same counterparty, a legal right of set-off exists and the cash flows are intended to be settled on a net basis.

Use of derivatives

HSBC transacts derivatives for three primary purposes: to create risk management solutions for clients, to manage the portfolio risks arising from client business and to manage and hedge HSBC's own risks. Derivatives (except for derivatives which are designated as effective hedging instruments as defined in IAS 39) are held for trading. The held for trading classification includes two types of derivatives: those used in sales and trading activities, and those used for risk management purposes but which for various reasons do not meet the qualifying criteria for hedge accounting. The second category includes derivatives managed in conjunction with financial instruments designated at fair value. These activities are described more fully below.

HSBC's derivative activities give rise to significant open positions in portfolios of derivatives. These positions are managed constantly to ensure that they remain within acceptable risk levels, with matching deals being utilised to achieve this where necessary. When entering into derivative transactions, HSBC employs the same credit risk management procedures to assess and approve potential credit exposures that are used for traditional lending.

Trading derivatives

Most of HSBC's derivative transactions relate to sales and trading activities. Sales activities include the structuring and marketing of derivative products to customers to enable them to take, transfer, modify or reduce current or expected risks. Trading activities in derivatives are entered into principally for the purpose of generating profits from short-term fluctuations in price or margin. Positions may be traded actively or be held over a period of time to benefit from expected changes in exchange rates, interest rates, equity prices or other market parameters. Trading includes market-making, positioning and arbitrage activities. Market-making entails quoting bid and offer prices to other market participants for the purpose of generating revenues based on spread and volume; positioning means managing market risk positions in the expectation of benefiting from favourable movements in prices, rates or indices; arbitrage involves identifying and profiting from price differentials between markets and products.

As mentioned above, other derivatives classified as held for trading include non-qualifying hedging derivatives, ineffective hedging derivatives and the components of hedging derivatives that are excluded from assessing hedge effectiveness. Non-qualifying hedging derivatives are entered into for risk management purposes but do not meet the criteria for hedge accounting. These include derivatives managed in conjunction with financial instruments designated at fair value.

Gains and losses from changes in the fair value of derivatives, including the contractual interest, that do not qualify for hedge accounting are reported in 'Net trading income', except for derivatives managed in conjunction with financial instruments designated at fair value, where gains and losses are reported in 'Net income from financial instruments designated at fair value', together with the gains and losses on the economically hedged items. Where the derivatives are managed with debt securities in issue, the contractual interest is shown in 'interest expense' together with the interest payable on the issued debt. Substantially all of HSBC Holdings' derivatives entered into with HSBC undertakings are managed in conjunction with financial liabilities designated at fair value.

The notional contract amounts of derivatives held for trading purposes indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk. The 27% increase in the notional amounts of HSBC's derivative assets during 2010 was primarily driven by an increase in the number of open interest rate contracts, reflecting increased trading volumes in the period.

Notes on the Financial Statements (continued)

Notional contract amounts of derivatives held for trading purposes by product type

	HSBC		HSBC Holdings	
	At 31 December 2010 US$m	At 31 December 2009 US$m	**At 31 December 2010 US$m**	At 31 December 2009 US$m
Foreign exchange	**3,692,798**	2,883,201	**17,287**	17,150
Interest rate	**18,104,141**	13,874,355	**6,804**	6,804
Equity	**294,587**	217,828	**–**	–
Credit	**1,065,218**	1,237,055	**–**	–
Commodity and other	**82,856**	53,720	**–**	–
	23,239,600	18,266,159	**24,091**	23,954

Credit derivatives

HSBC trades credit derivatives through its principal dealing operations and acts as a principal counterparty to a broad range of users, structuring deals to produce risk management products for its customers, or making markets in certain products. Risk is typically controlled through entering into offsetting credit derivative contracts with other counterparties.

HSBC manages the credit risk arising on buying and selling credit derivative protection by including the related credit exposures within its overall credit limit structure for the relevant counterparty. Trading of credit derivatives is restricted to a small number of offices within the major centres which have the control infrastructure and market skills to manage effectively the credit risk inherent in the products.

Credit derivatives are also deployed to a limited extent for the risk management of the Group's loan portfolios.

The notional contract amount of credit derivatives of US$1,065,218m (2009: US$1,237,055m) consisted of protection bought of US$530,235m (2009: US$614,690m) and protection sold of US$534,983m (2009: US$622,365m).

The credit derivative business operates within the market risk management framework described on pages 145 to 154.

Derivatives valued using models with unobservable inputs

The difference between the fair value at initial recognition (the transaction price) and the value that would have been derived had valuation techniques used for subsequent measurement been applied at initial recognition, less subsequent releases, is as follows:

Unamortised balance of derivatives valued using models with significant unobservable inputs

	2010 US$m	2009 US$m
Unamortised balance at 1 January	**260**	204
Deferral on new transactions	**331**	192
Recognised in the income statement during the period:		
– amortisation	**(106)**	(86)
– subsequent to unobservable inputs becoming observable	**(17)**	(19)
– maturity, termination or offsetting derivative	**(163)**	(42)
Exchange differences	**(15)**	11
Risk hedged	**(40)**	–
Unamortised balance at 31 December[1]	**250**	260

1 *This amount is yet to be recognised in the consolidated income statement.*

Hedging instruments

HSBC uses derivatives (principally interest rate swaps) for hedging purposes in the management of its own asset and liability portfolios and structural positions. This enables HSBC to optimise the overall cost to the Group of accessing debt capital markets, and to mitigate the market risk which would otherwise arise from structural imbalances in the maturity and other profiles of its assets and liabilities.

The accounting treatment of hedge transactions varies according to the nature of the instrument hedged and the type of hedge transactions. Derivatives may qualify as hedges for accounting purposes if they are fair value hedges, cash flow hedges, or hedges in net investment of foreign operations. These are described under the relevant headings below.

The notional contract amounts of derivatives held for hedging purposes indicate the nominal value of transactions outstanding at the balance sheet date; they do not represent amounts at risk.

Notional contract amounts of derivatives held for hedging purposes by product type

	At 31 December 2010		At 31 December 2009	
	Cash flow hedge US$m	**Fair value hedge US$m**	Cash flow hedge US$m	Fair value hedge US$m
Foreign exchange	**10,599**	**1,392**	12,359	2,469
Interest rate	**282,412**	**62,757**	236,388	42,224
	293,011	**64,149**	248,747	44,693

Fair value hedges

HSBC's fair value hedges principally consist of interest rate swaps that are used to protect against changes in the fair value of fixed-rate long-term financial instruments due to movements in market interest rates. For qualifying fair value hedges, all changes in the fair value of the derivative and in the fair value of the item in relation to the risk being hedged are recognised in the income statement. If the hedge relationship is terminated, the fair value adjustment to the hedged item continues to be reported as part of the basis of the item and is amortised to the income statement as a yield adjustment over the remainder of the hedging period.

Fair value of derivatives designated as fair value hedges

	At 31 December 2010		At 31 December 2009	
	Assets US$m	**Liabilities US$m**	Assets US$m	Liabilities US$m
Foreign exchange	**153**	**–**	342	–
Interest rate	**443**	**2,226**	242	1,085
	596	**2,226**	584	1,085

Gains or losses arising from fair value hedges

	2010 US$m	2009 US$m	2008 US$m
Gains/(losses):			
– on hedging instruments	**(830)**	114	(296)
– on the hedged items attributable to the hedged risk	**868**	(159)	301
	38	(45)	5

The gains and losses on ineffective portions of fair value hedges are recognised immediately in 'Net trading income'.

Cash flow hedges

HSBC's cash flow hedges consist principally of interest rate and cross-currency swaps that are used to protect against exposures to variability in future interest cash flows on non-trading assets and liabilities which bear interest at variable rates or which are expected to be re-funded or reinvested in the future. The amounts and timing of future cash flows, representing both principal and interest flows, are projected for each portfolio of financial assets and liabilities on the basis of their contractual terms and other relevant factors, including estimates of prepayments and defaults. The aggregate principal balances and interest cash flows across all portfolios over time form the basis for identifying gains and losses on the effective portions of derivatives designated as cash flow hedges of forecast transactions. Gains and losses are initially recognised in other comprehensive income, and accumulated in the cash flow hedging reserve, and are transferred to the income statement when the forecast cash flows affect the income statement.

Notes on the Financial Statements (continued)

Fair value of derivatives designated as cash flow hedges

	At 31 December 2010		At 31 December 2009	
	Assets US$m	**Liabilities US$m**	Assets US$m	Liabilities US$m
Foreign exchange	**1,151**	**340**	1,353	300
Interest rate	**2,321**	**1,683**	3,264	2,189
	3,472	**2,023**	4,617	2,489

Forecast principal balances on which interest cash flows are expected to arise

	3 months or less US$m	**More than 3 months but less than 1 year US$m**	**5 years or less but more than 1 year US$m**	**More than 5 years US$m**
At 31 December 2010				
Assets	**163,006**	**97,174**	**58,975**	**1,358**
Liabilities	**(89,112)**	**(58,811)**	**(42,259)**	**(6,065)**
Net cash inflows/(outflows) exposure	**73,894**	**38,363**	**16,716**	**(4,707)**
At 31 December 2009				
Assets	120,915	111,456	53,184	476
Liabilities	(71,143)	(78,841)	(39,377)	(6,559)
Net cash inflows/(outflows) exposure	49,772	32,615	13,807	(6,083)

This table reflects the interest rate repricing profile of the underlying hedged items.

The gains and losses on ineffective portions of such derivatives are recognised immediately in 'Net trading income'. During the year to 31 December 2010 a loss of US$9m (2009: gain of US$90m; 2008: loss of US$40m) was recognised due to hedge ineffectiveness.

Hedges of net investments in foreign operations

The Group applies hedge accounting in respect of certain consolidated net investments. Hedging is undertaken using forward foreign exchange contracts or by financing with currency borrowings.

At 31 December 2010, the fair values of outstanding financial instruments designated as hedges of net investments in foreign operations were liabilities of US$34m (2009: US$28m) and notional contract values of US$644m (2009: US$566m).

The ineffectiveness recognised in 'Net trading income' in the year ended 31 December 2010 that arose from hedges in foreign operations was nil (2009 and 2008: nil).

21 Financial investments

	2010 US$m	2009 US$m
Financial investments:		
– not subject to repledge or resale by counterparties	**369,597**	356,864
– which may be repledged or resold by counterparties	**31,158**	12,294
	400,755	369,158

Carrying amount and fair value of financial investments

	2010		2009	
	Carrying amount US$m	**Fair value US$m**	Carrying amount US$m	Fair value US$m
Treasury and other eligible bills	**57,129**	**57,129**	58,434	58,434
– available for sale	**57,016**	**57,016**	58,333	58,333
– held to maturity	**113**	**113**	101	101
Debt securities	**335,643**	**336,632**	301,600	302,171
– available for sale	**316,257**	**316,257**	284,074	284,074
– held to maturity	**19,386**	**20,375**	17,526	18,097
Equity securities	**7,983**	**7,983**	9,124	9,124
– available for sale	**7,983**	**7,983**	9,124	9,124
Total financial investments	**400,755**	**401,744**	369,158	369,729

Financial investments at amortised cost and fair value

	Amortised cost US$m	**Fair value[1] US$m**
At 31 December 2010		
US Treasury	**37,380**	**37,255**
US Government agencies[2]	**20,895**	**21,339**
US Government sponsored entities[2]	**5,029**	**5,267**
UK Government	**31,069**	**31,815**
Hong Kong Government	**29,770**	**29,793**
Other government	**108,947**	**109,806**
Asset-backed securities[3]	**39,845**	**33,175**
Corporate debt and other securities	**124,704**	**125,311**
Equities	**5,605**	**7,983**
	403,244	**401,744**
At 31 December 2009		
US Treasury	17,650	17,635
US Government agencies[2]	12,539	12,804
US Government sponsored entities[2]	4,885	4,924
UK Government	9,653	9,782
Hong Kong Government	37,747	37,763
Other government	87,122	87,881
Asset-backed securities[3]	48,500	34,914
Corporate debt and other securities	153,639	154,902
Equities	7,051	9,124
	378,786	369,729
At 31 December 2008		
US Treasury	11,528	11,755
US Government agencies[2]	8,131	8,307
US Government sponsored entities[2]	15,109	15,240
UK Government	16,077	16,217
Hong Kong Government	966	989
Other government	60,755	61,528
Asset-backed securities[3]	55,685	36,052
Corporate debt and other securities	145,269	143,940
Equities	5,901	7,251
	319,421	301,279

1 *Included within the above figures are debt securities issued by banks and other financial institutions of US$99,733m (2009: US$133,256m; 2008: US$140,878m), of which US$38,862m (2009: US$55,324m; 2008: US$39,213m) are guaranteed by various governments. The fair value of the debt securities issued by banks and other financial institutions was US$100,070m (2009: US$133,461m; 2008: US$141,526m).*
2 *Includes securities that are supported by an explicit guarantee issued by the US Government.*
3 *Excludes asset-backed securities included under US Government agencies and sponsored entities.*

Notes on the Financial Statements (continued)

21 – Financial investments / 22 – Transfers of financial assets not qualifying for derecognition

Financial investments listed on a recognised exchange and unlisted

	Treasury and other eligible bills available for sale US$m	Treasury and other eligible bills held to maturity US$m	Debt securities available for sale US$m	Debt securities held to maturity US$m	Equity securities available for sale US$m	Total US$m
Carrying amount at 31 December 2010						
Listed on a recognised exchange[1]	**1,400**	**–**	**138,374**	**4,182**	**851**	**144,807**
Unlisted[2]	**55,616**	**113**	**177,883**	**15,204**	**7,132**	**255,948**
	57,016	**113**	**316,257**	**19,386**	**7,983**	**400,755**
Carrying amount at 31 December 2009						
Listed on a recognised exchange[1]	2,334	–	135,653	2,743	911	141,641
Unlisted[2]	55,999	101	148,421	14,783	8,213	227,517
	58,333	101	284,074	17,526	9,124	369,158

1 *The fair value of listed held-to-maturity debt securities as at 31 December 2010 was US$4,332m (2009: US$2,769m). Included within listed investments were US$1,902m (2009: US$1,670m) of investments listed in Hong Kong.*
2 *Unlisted treasury and other eligible bills available for sale primarily comprise treasury bills not listed on a recognised exchange but for which there is a liquid market.*

Maturities of investments in debt securities at their carrying amount

	At 31 December 2010 US$m	At 31 December 2009 US$m
Remaining contractual maturity of total debt securities:		
1 year or less	**92,961**	75,782
5 years or less but over 1 year	**124,596**	141,683
10 years or less but over 5 years	**56,926**	31,934
Over 10 years	**61,160**	52,201
	335,643	301,600
Remaining contractual maturity of debt securities available for sale:		
1 year or less	**91,939**	75,160
5 years or less but over 1 year	**117,931**	135,187
10 years or less but over 5 years	**50,113**	26,105
Over 10 years	**56,274**	47,622
	316,257	284,074
Remaining contractual maturity of debt securities held to maturity:		
1 year or less	**1,022**	622
5 years or less but over 1 year	**6,665**	6,496
10 years or less but over 5 years	**6,813**	5,829
Over 10 years	**4,886**	4,579
	19,386	17,526

Contractual maturities and weighted average yields of investment debt securities at 31 December 2010

	Within one year		After one year but within five years		After five years but within ten years		After ten years	
	Amount US$m	Yield %	Amount US$m	Yield %	Amount US$m	Yield %	Amount US$m	Yield %
Available-for-sale								
US Treasury	**8,761**	**0.95**	**13,513**	**1.19**	**9,225**	**2.61**	**4,648**	**4.32**
US Government agencies	**–**	**–**	**7**	**2.95**	**230**	**4.78**	**20,236**	**3.71**
US Government-sponsored agencies	**859**	**0.70**	**114**	**1.75**	**1,993**	**3.81**	**445**	**3.60**
UK Government	**3,994**	**2.90**	**11,407**	**2.22**	**13,987**	**2.97**	**1,248**	**2.80**
Hong Kong Government	**362**	**0.55**	**407**	**2.95**	**–**	**–**	**–**	**–**
Other governments	**28,779**	**2.25**	**44,920**	**4.00**	**6,945**	**4.65**	**2,073**	**4.58**
Asset-backed securities	**392**	**0.77**	**2,311**	**1.73**	**7,773**	**0.66**	**29,178**	**0.64**
Corporate debt and other securities	**49,014**	**2.26**	**44,009**	**2.54**	**10,342**	**3.44**	**4,065**	**4.72**
Total amortised cost	**92,161**		**116,688**		**50,495**		**61,893**	
Total carrying value	**91,939**		**117,931**		**50,113**		**56,274**	

	Within one year		After one year but within five years		After five years but within ten years		After ten years	
	Amount US$m	Yield %	Amount US$m	Yield %	Amount US$m	Yield %	Amount US$m	Yield %
Held-to-maturity								
US Treasury	–	–	32	3.13	60	6.67	62	9.68
US Government agencies	–	–	–	–	6	7.65	416	6.49
US Government-sponsored agencies	19	5.26	28	7.14	2	6.92	1,560	6.15
Hong Kong Government	2	3.02	–	–	8	5.05	–	–
Other governments	53	5.66	424	3.30	252	4.37	595	7.23
Asset-backed securities	–	–	–	–	–	–	191	6.28
Corporate debt and other securities	948	4.01	6,181	4.29	6,485	4.52	2,062	5.92
Total amortised cost	1,022		6,665		6,813		4,886	
Total carrying value	1,022		6,665		6,813		4,886	

The maturity distributions of asset-backed securities are presented in the above table on the basis of contractual maturity dates. The weighted average yield for each range of maturities is calculated by dividing the annualised interest income for the year ended 31 December 2010 by the book amount of available-for-sale debt securities at that date. The yields do not include the effect of related derivatives.

22 Transfers of financial assets not qualifying for derecognition

HSBC enters into transactions in the normal course of business by which it transfers recognised financial assets directly to third parties or to SPEs. These transfers may give rise to the full or partial derecognition of the financial assets concerned.

- Full derecognition occurs when HSBC transfers its contractual right to receive cash flows from the financial assets, or retains the right but assumes an obligation to pass on the cash flows from the asset, and transfers substantially all the risks and rewards of ownership. The risks include credit, interest rate, currency, prepayment and other price risks.
- Partial derecognition occurs when HSBC sells or otherwise transfers financial assets in such a way that some but not substantially all of the risks and rewards of ownership are transferred but control is retained. These financial assets are recognised on the balance sheet to the extent of HSBC's continuing involvement.

The majority of financial assets that do not qualify for derecognition are (i) debt securities held by counterparties as collateral under repurchase agreements or (ii) equity securities lent under securities lending agreements. The following table analyses the carrying amount of financial assets that did not qualify for derecognition and their associated financial liabilities:

Financial assets and associated financial liabilities not qualifying for derecognition

	2010		2009	
	Carrying amount of transferred assets US$m	**Carrying amount of associated liabilities US$m**	Carrying amount of transferred assets US$m	Carrying amount of associated liabilities US$m
Nature of transaction				
Repurchase agreements	**124,625**	**122,455**	108,518	107,525
Securities lending agreements	**7,277**	**7,202**	7,363	7,264
	131,902	**129,657**	115,881	114,789

A small proportion of financial assets that do not qualify for derecognition relate to loans, credit cards, debt securities and trade receivables that have been securitised under arrangements by which HSBC retains a continuing involvement in such transferred assets. Continuing involvement may entail retaining the rights to future cash flows arising from the assets after investors have received their contractual terms (for example, interest rate strips); providing subordinated interest; liquidity support; continuing to service the underlying asset; or entering into derivative transactions with the securitisation vehicles. As such, HSBC continues to be exposed to risks associated with these transactions.

The rights and obligations that HSBC retains from its continuing involvement in securitisations are initially recorded as an allocation of the fair value of the financial asset between the part that is derecognised and the part that continues to be recognised on the date of transfer. The following table analyses the carrying amount of financial assets that qualified for partial derecognition, the extent of HSBC's continuing involvement and the associated liabilities:

HSBC's continuing involvement in financial assets qualifying for partial derecognition

	Securitisations at 31 December	
	2010	2009
	US$m	US$m
Carrying amount of assets (original)	**17,427**	17,427
Carrying amount of assets (currently recognised)	**42**	139
Carrying amount of associated liabilities (currently recognised)	**21**	69

23 Interests in associates and joint ventures

Associates

Principal associates of HSBC

	At 31 December 2010		At 31 December 2009	
	Carrying amount	**Fair value**	Carrying amount	Fair value
	US$m	**US$m**	US$m	US$m
Listed				
Bank of Communications Co., Limited	**6,944**	**10,773**	5,110	10,820
Industrial Bank Co., Limited	**1,769**	**2,799**	1,084	3,774
Ping An Insurance (Group) Company of China, Limited	**5,596**	**13,735**	4,391	10,803
SABB Takaful Company	**28**	**49**	29	99
The Saudi British Bank	**1,580**	**3,224**	1,376	3,472
	15,917	**30,580**	11,990	28,968

	At 31 December 2010		
	Country of incorporation	**HSBC's interest in equity capital**	**Issued equity capital**
Listed			
Bank of Communications Co., Limited	**PRC[1]**	**19.03%**	**RMB56,260m**
Industrial Bank Co., Limited	**PRC[1]**	**12.80%**	**RMB5,992m**
Ping An Insurance (Group) Company of China, Limited	**PRC[1]**	**16.13%**	**RMB7,345m**
SABB Takaful Company	**Saudi Arabia**	**32.50%**	**SR340m**
The Saudi British Bank	**Saudi Arabia**	**40.00%**	**SR7,500m**
Unlisted			
Barrowgate Limited[3]	**Hong Kong**	**24.64%**	**–**
Vietnam Technological and Commercial Joint Stock Bank	**Vietnam**	**19.79%**	**VND6,932,184m**
Yantai Bank Co., Limited[2]	**PRC[1]**	**20.00%**	**RMB2,000m**

1 *People's Republic of China.*
2 *Yantai Bank Co., Limited was previously known as Yantai City Commercial Bank. The investment is held through Hang Seng Bank Limited, a 62.14% owned subsidiary of HSBC.*
3 *Issued equity capital is less than HK$1m.*

All the above investments in associates are owned by subsidiaries of HSBC Holdings.

During 2010, HSBC disposed of its 48.92% interest in the equity capital of British Arab Commercial Bank Public Limited Company, which was previously reported as an unlisted principal associate.

Details of all HSBC associates and joint ventures, as required under Section 409 Companies Act 2006, will be annexed to the next Annual Return of HSBC Holdings filed with the UK Registrar of Companies.

HSBC had US$12,540m (2009: US$9,501m) of investments in associates and joint ventures listed in Hong Kong.

For the year ended 31 December 2010, HSBC's share of associates and joint ventures' tax on profit was US$774m (2009: US$491m), which is included within share of profit in associates and joint ventures in the income statement.

Summarised aggregate financial information on associates

	2010 US$m	2009 US$m
HSBC's share of:		
– assets	**191,286**	158,890
– liabilities	**175,812**	147,501
– revenues	**9,274**	7,514
– profit after tax	**2,479**	1,735

HSBC's investment in Bank of Communications Co., Limited was equity accounted with effect from August 2004. HSBC's significant influence in Bank of Communications Co., Limited was established as a result of representation on the Board of Directors, and in accordance with the Technical Support and Assistance Agreements, HSBC is assisting in the development of financial and operating policies and a number of staff have been seconded to assist in this process.

HSBC's investment in Industrial Bank Co., Limited was equity accounted with effect from May 2004, reflecting HSBC's significant influence over this associate. HSBC's significant influence was established as a result of representation on the Board of Directors, and in accordance with the Technical Support and Assistance Agreements, HSBC is assisting in the development of financial and operating policies.

HSBC's investment in Ping An Insurance (Group) Company of China, Limited was equity accounted with effect from 31 August 2005, reflecting HSBC's significant influence over this associate. HSBC's significant influence was established as a result of representation on the Board of Directors. In May 2010, following the issue of shares by the associate to a third party, HSBC's holding was diluted to 16.13% and a dilution gain of US$188m was recognised in 'Other operating income'.

The statutory accounting reference date of Bank of Communications Co., Limited, Ping An Insurance (Group) Company of China, Limited and Industrial Bank Co., Limited is 31 December. For the year ended 31 December 2010, these companies were included on the basis of financial statements made up for the twelve months to 30 September 2010, taking into account changes in the subsequent period from 1 October 2010 to 31 December 2010 that would have materially affected their results.

HSBC acquired 15% of Vietnam Technological & Commercial Joint Stock Bank in October 2007. This investment was equity accounted from that date due to HSBC's representation on the Board of Directors and involvement in the Technical Support and Assistance Agreement. In December 2007, as a result of a rights issue in which HSBC did not participate, HSBC's equity interest was diluted to 14.44%. In September 2008, HSBC increased its equity interest to 20%. HSBC's equity interest has been subsequently diluted to below 20% due to the issue of shares by the associate to its own employees.

Joint ventures

Principal interests in joint ventures

	At 31 December 2010			
	Country of incorporation	**Principal activity**	**HSBC's interest in equity capital**	**Issued equity capital**
HSBC Saudi Arabia Limited	**Saudi Arabia**	**Investment banking**	**60.00%**	**SR50m**
Vaultex UK Limited	**England**	**Cash management**	**50.00%**	**£10m**
Hana HSBC Life Insurance Co., Ltd	**South Korea**	**Insurance manufacturing**	**49.99%**	**KRW60,201m**
Canara HSBC Oriental Bank of Commerce Life Insurance Company Limited	**India**	**Insurance manufacturing**	**26.00%**	**INR5,000m**

Notes on the Financial Statements (continued)

Summarised aggregate financial information on joint ventures

	2010 US$m	2009 US$m
HSBC's share of:		
– current assets	**1,481**	700
– non-current assets	**97**	513
– current liabilities	**706**	621
– non-current liabilities	**666**	416
– income	**366**	370
– expenses	**328**	324

Goodwill included in carrying amount of associates and joint ventures

	2010 US$m	2009 US$m
Gross amount		
At 1 January	**1,446**	1,453
Additions	**60**	5
Exchange differences	**40**	(12)
Other changes	**(28)**	–
At 31 December[1]	**1,518**	1,446

1 *Includes the carrying amount of goodwill arising from joint ventures of US$32m (2009: US$32m).*

24 Goodwill and intangible assets

	2010 US$m	2009 US$m
Goodwill	**22,406**	23,241
Present value of in-force long-term insurance business ('PVIF')[1]	**3,440**	2,780
Other intangible assets	**4,076**	3,973
	29,922	29,994

1 *Disclosures on PVIF are provided on page 170.*

Goodwill

Reconciliation of goodwill

	Europe US$m	Hong Kong US$m	Rest of Asia-Pacific US$m	Middle East US$m	North America US$m	Latin America US$m	Total US$m
Gross amount							
At 1 January 2010	**15,915**	**123**	**1,053**	**69**	**12,483**	**4,162**	**33,805**
Additions	**–**	**–**	**16**	**–**	**–**	**–**	**16**
Disposals	**(3)**	**–**	**–**	**–**	**(17)**	**–**	**(20)**
Exchange differences	**(1,004)**	**1**	**52**	**(4)**	**(1)**	**154**	**(802)**
Other changes	**(23)**	**–**	**(6)**	**–**	**–**	**–**	**(29)**
At 31 December 2010	**14,885**	**124**	**1,115**	**65**	**12,465**	**4,316**	**32,970**
Accumulated impairment losses							
At 1 January and 31 December 2010	**–**	**–**	**–**	**–**	**(10,564)**	**–**	**(10,564)**
Net carrying amount at 31 December 2010	**14,885**	**124**	**1,115**	**65**	**1,901**	**4,316**	**22,406**

	Europe US$m	Hong Kong US$m	Rest of Asia-Pacific US$m	Middle East US$m	North America US$m	Latin America US$m	Total US$m
Gross amount							
At 1 January 2009	15,511	122	364	69	12,487	3,866	32,419
Additions	–	–	570	–	–	10	580
Disposals	(3)	–	–	–	–	–	(3)
Exchange differences	460	1	119	–	–	294	874
Other changes	(53)	–	–	–	(4)	(8)	(65)
At 31 December 2009	15,915	123	1,053	69	12,483	4,162	33,805
Accumulated impairment losses							
At 1 January and 31 December 2009	–	–	–	–	(10,564)	–	(10,564)
Net carrying amount at 31 December 2009	15,915	123	1,053	69	1,919	4,162	23,241

During 2010, there was no impairment of goodwill (2009: nil; 2008: US$10.6bn).

Impairment testing

Timing of impairment testing

HSBC's impairment test in respect of goodwill allocated to each cash-generating unit ('CGU') is performed as at 1 July each year. In line with the accounting policy set out in Note 2p, goodwill is also retested for impairment whenever there is an indication that goodwill may be impaired. There was no indication of impairment in the period to 31 December 2010 and therefore goodwill has not been retested since 1 July 2010. For the purpose of impairment testing, the Group's CGUs are based on customer groups and global business separated by geographical region. The CGUs represent the lowest level at which goodwill is monitored for internal management purposes.

Basis of the recoverable amount – value in use or fair value less costs to sell

The recoverable amount of all CGUs to which goodwill has been allocated was equal to its value in use ('VIU') at each respective testing date for 2009 and 2010.

For each significant CGU, the VIU is calculated by discounting management's cash flow projections for the CGU. The discount rate used is based on the cost of capital HSBC allocates to investments in the countries within which the CGU operates. The long-term growth rate is used to extrapolate the cash flows in perpetuity because of the long-term perspective within the Group of the business units making up the CGUs. In 2010, for most CGUs, management's cash flow projections until the end of 2011 were used. However, due to the current economic conditions in Personal Financial Services – Latin America, a 10-year cash flow projection was used to more accurately estimate the cash flows for the period.

Key assumptions in VIU calculation and management's approach to determining the values assigned to each key assumption

	2010			2009		
Cash-generating unit	**Goodwill at 1 July 2010 US$m**	**Discount rate %**	**Nominal growth rate beyond initial cash flow projections %**	Goodwill at 1 July 2009 US$m	Discount rate %	Nominal growth rate beyond initial cash flow projections %
Personal Financial Services – Europe	**4,017**	**11.0**	**3.0**	4,507	11.0	3.1
Commercial Banking – Europe	**3,015**	**11.0**	**3.0**	3,480	11.0	3.1
Global Private Banking – Europe	**4,055**	**11.0**	**3.0**	4,483	11.0	3.1
Global Banking and Markets – Europe	**2,983**	**12.0**	**3.0**	3,489	11.0	3.1
Personal Financial Services – Latin America	**2,385**	**14.3**	**8.6**	2,350	15.0	8.0
Total goodwill in the CGUs listed above	**16,455**			18,309		

Notes on the Financial Statements (continued)

At 1 July 2010, aggregate goodwill of US$4,674m (1 July 2009: US$4,475m) had been allocated to CGUs that were not considered individually significant. These CGUs do not carry on their balance sheets any significant intangible assets with indefinite useful lives, other than goodwill.

Nominal long-term growth rate: external data that reflects the market's assessment of GDP and inflation for the countries within which the CGU operates. The rates used for 2009 and 2010 are taken as an average of the last 10 years.

Discount rate: the discount rate used to discount the cash flows is based on the cost of capital assigned to each CGU, which is derived using a Capital Asset Pricing Model ('CAPM'). The CAPM depends on inputs reflecting a number of financial and economic variables including the risk-free rate in the country concerned and a premium to reflect the inherent risk of the business being evaluated. These variables are based on the market's assessment of the economic variables and management's judgement. In addition, for the purposes of testing goodwill for impairment, management supplements this process by comparing the discount rates derived using the internally generated CAPM with cost of capital rates produced by external sources. HSBC uses externally-sourced cost of capital rates where, in management's judgement, those rates reflect more accurately the current market and economic conditions. For 2010 and 2009, internal costs of capital rates were consistent with externally-sourced rates.

Management's judgement in estimating the cash flows of a CGU: the cash flow projections for each CGU are based on plans approved by the Group Management Board. The key assumptions in addition to the discount rate and nominal long-term growth rate for each significant CGU are discussed below.

Personal Financial Services – Europe and Commercial Banking – Europe: the assumptions included in the cash flow projections for Personal Financial Services – Europe and Commercial Banking – Europe reflect the economic environment and financial outlook of the European countries within these two segments. Key assumptions include the level of interest rates and the level and change in unemployment rates. While current economic conditions in Europe continue to be challenging, management's cash flow projections are based primarily on these prevailing conditions. Risks include a double-dip recession in the UK and the continuation of base rates at their current low levels. Based on the conditions at the balance sheet date, management determined that a reasonably possible change in any of the key assumptions described above would not cause an impairment to be recognised in respect of Personal Financial Services – Europe or Commercial Banking – Europe.

Global Private Banking – Europe: the revenues in Global Private Banking – Europe are predominately generated through HSBC's client relationships. The cash flow forecast reflects current economic conditions and key assumptions include the level of interest rates and client risk appetite. Further economic deterioration could result in a decrease in assets under management and a reduction in fee and trading income through increased client risk aversion. Based on the conditions at the balance sheet date, management determined that a reasonably possible change in any of the key assumptions described above would not cause an impairment to be recognised in respect of Global Private Banking – Europe.

Global Banking and Markets – Europe: the cash flows generated by Global Banking and Markets – Europe are diversified and there is no one key assumption that drives the cash flow projection of this CGU. In line with other CGUs, Global Banking and Markets – Europe is sensitive to changes in the interest rate environment and the strength of economic recovery in Europe. One of the key factors which may impact the carrying value of this CGU is the level of impairment charges which may emerge in the future, particularly in respect of holdings of available-for-sale sub-prime and Alt-A Residential MBSs. Based on management's current assessment of the credit quality of these securities, which includes stressed scenarios for collateral defaults and house prices, and the level of credit support available, management determined that a reasonably possible change in key assumptions would not cause an impairment to be recognised in respect of Global Banking and Markets – Europe.

Personal Financial Services – Latin America: the assumptions included in the cash flow projections for Personal Financial Services – Latin America reflect the economic environment and financial outlook of the countries within this segment, with Brazil and Mexico being two of the largest countries included within this segment. Key assumptions include the growth in lending and deposit volumes and the credit quality of the loan portfolios. Mexico and Central America in particular are sensitive to economic conditions in the US which could constrain demand. Based on the conditions at the balance sheet date, management determined that a reasonably possible change in any of the key assumptions described above would not cause an impairment to be recognised in respect of Personal Financial Services – Latin America.

Other intangible assets

Movement of intangible assets excluding goodwill and the PVIF

	Trade names US$m	Mortgage servicing rights US$m	Internally generated software US$m	Purchased software US$m	Customer/ merchant relation-ships US$m	Other US$m	Total US$m
Cost							
At 1 January 2010	**68**	**689**	**4,400**	**954**	**1,988**	**502**	**8,601**
Additions[1]	**–**	**52**	**960**	**140**	**48**	**4**	**1,204**
Disposals	**–**	**(105)**	**(40)**	**(15)**	**(79)**	**–**	**(239)**
Amount written off	**–**	**–**	**(70)**	**(2)**	**–**	**–**	**(72)**
Exchange differences	**–**	**–**	**(68)**	**(4)**	**30**	**27**	**(15)**
Other changes	**–**	**–**	**20**	**(8)**	**–**	**(30)**	**(18)**
At 31 December 2010	**68**	**636**	**5,202**	**1,065**	**1,987**	**503**	**9,461**
Accumulated amortisation							
At 1 January 2010	**(50)**	**(240)**	**(2,511)**	**(747)**	**(955)**	**(125)**	**(4,628)**
Charge for the year[2]	**(5)**	**(105)**	**(596)**	**(97)**	**(243)**	**(30)**	**(1,076)**
Impairment	**–**	**–**	**(12)**	**–**	**–**	**–**	**(12)**
Disposals	**–**	**105**	**33**	**8**	**68**	**(1)**	**213**
Amount written off	**–**	**–**	**70**	**2**	**–**	**–**	**72**
Exchange differences	**1**	**–**	**48**	**1**	**(13)**	**(1)**	**36**
Other changes	**2**	**–**	**10**	**(15)**	**–**	**13**	**10**
At 31 December 2010	**(52)**	**(240)**	**(2,958)**	**(848)**	**(1,143)**	**(144)**	**(5,385)**
Net carrying amount at 31 December 2010	**16**	**396**	**2,244**	**217**	**844**	**359**	**4,076**
Cost							
At 1 January 2009	67	1,360	3,429	867	1,749	421	7,893
Additions[1]	–	116	763	65	20	10	974
Acquisition of subsidiaries	–	–	–	–	58	–	58
Disposals	–	(29)	(14)	(18)	(25)	–	(86)
Amount written off	–	(757)	(45)	(1)	(15)	–	(818)
Exchange differences	1	–	247	53	201	9	511
Other changes	–	(1)	20	(12)	–	62	69
At 31 December 2009	68	689	4,400	954	1,988	502	8,601
Accumulated amortisation							
At 1 January 2009	(45)	(1,023)	(1,992)	(631)	(681)	(52)	(4,424)
Charge for the year[2]	(4)	(3)	(433)	(98)	(228)	(30)	(796)
Impairment	–	–	(6)	(5)	(6)	–	(17)
Disposals	–	29	6	18	15	–	68
Amount written off	–	757	45	1	15	–	818
Exchange differences	(1)	–	(131)	(32)	(72)	(1)	(237)
Other changes	–	–	–	–	2	(42)	(40)
At 31 December 2009	(50)	(240)	(2,511)	(747)	(955)	(125)	(4,628)
Net carrying amount at 31 December 2009	18	449	1,889	207	1,033	377	3,973

1 *At 31 December 2010, HSBC had US$0.2m (2009: US$0.2m) of contractual commitments to acquire intangible assets.*
2 *The amortisation charge for the year is recognised within the income statement under 'Amortisation and impairment of intangible assets', with the exception of the amortisation of mortgage servicing rights which is recognised in net fee income.*

25 Property, plant and equipment

	Freehold land and buildings US$m	Long leasehold land and buildings US$m	Short leasehold land and buildings[1] US$m	Equipment, fixtures and fittings[2] US$m	Equipment on operating leases US$m	Total[3] US$m
Cost or fair value						
At 1 January 2010	**3,915**	**1,327**	**3,135**	**11,552**	**5,236**	**25,165**
Additions at cost[4]	**349**	**76**	**632**	**1,456**	**65**	**2,578**
Fair value adjustments	**31**	**24**	**38**	**–**	**–**	**93**
Disposals[5]	**(307)**	**(8)**	**(82)**	**(355)**	**(5,113)**	**(5,865)**
Reclassified to held for sale	**(73)**	**(16)**	**(3)**	**(35)**	**–**	**(127)**
Transfers	**(47)**	**(147)**	**199**	**(5)**	**–**	**–**
Exchange differences	**(47)**	**(5)**	**(17)**	**(62)**	**(135)**	**(266)**
Other changes	**131**	**422**	**102**	**(22)**	**–**	**633**
At 31 December 2010	**3,952**	**1,673**	**4,004**	**12,529**	**53**	**22,211**
Accumulated depreciation and impairment						
At 1 January 2010	**(450)**	**(229)**	**(1,065)**	**(7,743)**	**(1,876)**	**(11,363)**
Depreciation charge for the year	**(91)**	**(46)**	**(203)**	**(1,178)**	**(150)**	**(1,668)**
Disposals[5]	**31**	**–**	**68**	**344**	**1,956**	**2,399**
Reclassified (from)/to held for sale	**24**	**–**	**1**	**26**	**–**	**51**
Transfers	**23**	**20**	**(43)**	**–**	**–**	**–**
Impairment losses recognised	**(22)**	**–**	**1**	**(24)**	**–**	**(45)**
Exchange differences	**5**	**2**	**5**	**54**	**45**	**111**
Other changes	**(106)**	**(54)**	**(32)**	**15**	**2**	**(175)**
At 31 December 2010	**(586)**	**(307)**	**(1,268)**	**(8,506)**	**(23)**	**(10,690)**
Net carrying amount at 31 December 2010	**3,366**	**1,366**	**2,736**	**4,023**	**30**	**11,521**
Cost or fair value						
At 1 January 2009	4,126	1,736	2,924	10,320	4,547	23,653
Additions at cost[4]	344	35	179	1,253	299	2,110
Acquisition of subsidiaries	–	–	15	7	–	22
Fair value adjustments	(58)	16	18	–	–	(24)
Disposals	(201)	(510)	(98)	(640)	(117)	(1,566)
Reclassified to held for sale	(697)	–	(20)	(63)	–	(780)
Transfers	–	(2)	2	–	–	–
Exchange differences	342	62	90	737	507	1,738
Other changes	59	(10)	25	(62)	–	12
At 31 December 2009	3,915	1,327	3,135	11,552	5,236	25,165
Accumulated depreciation and impairment						
At 1 January 2009	(368)	(228)	(886)	(6,614)	(1,532)	(9,628)
Depreciation charge for the year	(82)	(44)	(193)	(1,160)	(169)	(1,648)
Disposals	39	46	90	495	(4)	666
Reclassified to held for sale	46	–	3	30	–	79
Impairment losses recognised	(30)	(1)	(26)	(20)	–	(77)
Exchange differences	(25)	(7)	(42)	(496)	(173)	(743)
Other changes	(30)	5	(11)	22	2	(12)
At 31 December 2009	(450)	(229)	(1,065)	(7,743)	(1,876)	(11,363)
Net carrying amount at 31 December 2009	3,465	1,098	2,070	3,809	3,360	13,802

1 *Including assets held on finance leases with a net book value of US$11m (2009: US$18m).*
2 *Including assets held on finance leases with a net book value of US$204m (2009: US$513m).*
3 *Including assets with a net book value of US$31m (2009: US$36m) pledged as security for liabilities.*
4 *At 31 December 2010, HSBC had US$593m (2009: US$878m) of contractual commitments to acquire property, plant and equipment.*
5 *The disposals included under 'Equipment on operating leases' relate to the sale of a subsidiary, Eversholt Rail Group, during the year.*

Leasehold land and buildings

Leasehold land and buildings are considered to be held under finance lease contracts where the value of the land cannot reliably be separated from the value of the lease and the respective contracts do not meet the criteria for classification as operating leases. Included within 'Short leasehold land and buildings' are the following amounts in respect of assets classed as improvements to buildings, which are carried at depreciated historical cost:

Leasehold land and buildings

	2010		2009	
	Cost	**Accumulated depreciation**	Cost	Accumulated depreciation
	US$m	**US$m**	US$m	US$m
At 1 January	**1,824**	**(831)**	1,621	(675)
Additions	**181**	**–**	175	–
Disposals	**(81)**	**54**	(89)	71
Depreciation charge for the year	**–**	**(133)**	–	(133)
Impairment loss recognised	**–**	**–**	–	(24)
Exchange differences	**(16)**	**–**	86	(40)
Other changes	**36**	**(23)**	31	(30)
At 31 December	**1,944**	**(933)**	1,824	(831)
Net carrying amount at 31 December	**1,011**		993	

Investment properties

Movement on the fair value of investment properties

	Freehold land and buildings US$m	Long leasehold land and buildings US$m	Short leasehold land and buildings US$m	Total US$m
Fair value				
At 1 January 2010	**640**	**184**	**237**	**1,061**
Additions at cost	**240**	**–**	**–**	**240**
Fair value adjustments	**31**	**24**	**38**	**93**
Disposals	**(216)**	**(2)**	**–**	**(218)**
Transfers	**–**	**(42)**	**42**	**–**
Exchange differences	**(34)**	**(1)**	**(1)**	**(36)**
Other changes	**6**	**(7)**	**(6)**	**(7)**
At 31 December 2010	**667**	**156**	**310**	**1,133**
Fair value				
At 1 January 2009	566	188	217	971
Additions at cost	36	–	–	36
Fair value adjustments	(58)	16	18	(24)
Disposals	–	(25)	–	(25)
Exchange differences	57	5	–	62
Other changes	39	–	2	41
At 31 December 2009	640	184	237	1,061

Investment properties are valued on an open market value basis as at 31 December each year by independent professional valuers who have recent experience in the location and type of properties. Investment properties in Hong Kong, the Macau Special Administrative Region and mainland China, which represent more than 35% by value of HSBC's investment properties subject to revaluation, were valued by an independent valuer who is a member of the Hong Kong Institute of Surveyors and who has recent experience in the locations and categories of the investment properties.

Included within 'Other operating income' was rental income of US$26m (2009: US$81m; 2008: US$23m) earned by HSBC on its investment properties. Direct operating expenses of US$3m (2009: US$2m; 2008: US$2m) incurred in respect of the investment properties during the year were recognised in 'General and administrative expenses'. Direct operating expenses arising in respect of investment properties that did not generate rental income during 2010 amounted to nil (2009 and 2008: nil).

At 31 December 2010, HSBC had no contractual obligations to purchase, construct, develop, maintain or enhance investment properties (2009: nil).

HSBC Holdings had no investment properties at 31 December 2010 or 2009.

HSBC properties leased to customers

HSBC properties leased to customers included US$441m at 31 December 2010 (2009: US$434m) let under operating leases, net of accumulated depreciation of US$19m (2009: US$18m). None was held by HSBC Holdings.

26 Investments in subsidiaries

Principal subsidiaries of HSBC Holdings

	At 31 December 2010			
	Country of incorporation or registration	HSBC's interest in equity capital %	Issued equity capital	Share class
Europe				
HSBC Asset Finance (UK) Limited	England	100	£265m	Ordinary £1
HSBC Bank A.S.	Turkey	100	TRL652m	A-Common TRL1 B-Common TRL1
HSBC Bank Malta p.l.c.	Malta	70.03	€88m	Ordinary €0.30
HSBC Bank plc	England	100	£797m	Ordinary £1 Preferred Ordinary £1 Series 2 Third Dollar Preference US$0.01 Third Dollar Preference US$0.01
HSBC France	France	99.99	€337m	Shares €5.00
HSBC Bank International Limited	Jersey	100	£1m	Ordinary £1
HSBC Life (UK) Limited	England	100	£94m	Ordinary £1
HSBC Private Banking Holdings (Suisse) S.A.	Switzerland	100	CHF1,363m	Ordinary CHF1,000
HSBC Trinkaus & Burkhardt AG	Germany	80.40	€28m	Shares of no par value
Marks and Spencer Retail Financial Services Holdings Limited	England	100	£67m	Ordinary £1
Hong Kong				
Hang Seng Bank Limited[7]	Hong Kong	62.14	HK$9,559m	Ordinary HK$5.00
HSBC Insurance (Asia) Limited	Hong Kong	100	HK$318m	Ordinary HK$1,000
HSBC Life (International) Limited	Bermuda	100	HK$421m	Ordinary HK$1.00
The Hongkong and Shanghai Banking Corporation Limited	Hong Kong	100	HK$22,494m	Ordinary HK$2.50 CIP[1] US$1.00 CRP[2] US$1.00 NIP[3] US$1.00
Rest of Asia-Pacific				
HSBC Bank Australia Limited	Australia	100	A$751m	Shares of no par value
HSBC Bank (China) Company Limited	PRC[4]	100	RMB8,000m	Ordinary CNY1.00
HSBC Bank Malaysia Berhad	Malaysia	100	RM115m	Ordinary RM0.50
Middle East				
HSBC Bank Middle East Limited	Jersey	100	US$931m	CRP[2] US$1.00 Ordinary US$1.00
HSBC Bank Egypt S.A.E.	Egypt	94.53	EGP1,511m	Ordinary EGP84.00
North America				
HSBC Bank Bermuda Limited	Bermuda	100	US$30m	Common BMD1.00
HSBC Bank Canada	Canada	100	C$1,225m	Class 1 Pref of NPV[5] Class 2 Pref of NPV[5] Common of NPV
HSBC Bank USA, N.A.	United States	100	US$2m	Common US$100
HSBC Finance Corporation	United States	100	–[6]	Common US$0.01
HSBC Securities (USA) Inc.	United States	100	–[6]	Common US$0.05
Latin America				
HSBC Bank Argentina S.A.	Argentina	99.99	ARS1,244m	Ordinary-A ARS1.00 Ordinary-B ARS1.00
HSBC Bank Brasil S.A. – Banco Múltiplo	Brazil	100	BRL5,178m	Shares of no par value
HSBC Mexico, S.A., Institución de Banca Múltiple, Grupo Financiero HSBC	Mexico	99.99	MXN5,087m	Ordinary MXN2.00
HSBC Bank (Panama) S.A.	Panama	100	US$10m	Ordinary PAB 1.00

1 *Cumulative Irredeemable Preference shares.*
2 *Cumulative Redeemable Preference shares*
3 *Non-cumulative Irredeemable Preference shares.*
4 *People's Republic of China*
5 *Preference shares of nil par value.*
6 *Issued equity capital is less than US$1m.*
7 *Listed in Hong Kong.*

Details of the debt, subordinated debt and preference shares issued by the principal subsidiaries to parties external to the Group are included in the Notes 30 'Debt securities in issue', 34 'Subordinated liabilities' and 38 'Non-controlling interests', respectively.

All the above subsidiaries are included in the HSBC consolidated financial statements.

Details of all HSBC subsidiaries will be annexed to the next Annual Return of HSBC Holdings filed with the UK Registrar of Companies.

All the above make their financial statements up to 31 December except for HSBC Bank Argentina S.A., whose financial statements are made up to 30 June annually.

The principal countries of operation are the same as the countries of incorporation except for HSBC Bank Middle East Limited which operates mainly in the Middle East and HSBC Life (International) Limited which operates mainly in Hong Kong.

Subsidiaries which experience significant restrictions on their ability to transfer funds to HSBC in the form of cash dividends or to repay loans and advances

During 2010 and 2009, none of the Group's subsidiaries experienced significant restrictions on paying dividends or repaying loans and advances.

Subsidiaries excluding SPEs where HSBC owns less than 50% of the voting rights

At 31 December 2009, HSBC consolidated HSBC Private Equity Fund 3 ('HPEF3') but only had a 38.8% interest in its equity capital. HSBC had control under IAS 27 because it was the investment adviser/manager of the fund and had a significant equity interest.

On 30 November 2010, the Group completed the sale of an 80.1% interest in HSBC Private Equity (Asia) Limited ('HPEA') to HPEA's management. As a result, the Group no longer controls HPEF3. The Group previously consolidated HPEF 3 by virtue of its control over HPEA, which in turn controlled HPEF3. Upon deconsolidation, the group retains its 38.8% interest in HPEF3 as an available for sale investment. HPEF3 has been renamed The Headland Private Equity Fund 3 Limited.

SPEs consolidated by HSBC where HSBC owns less than 50% of the voting rights

	Carrying value of total consolidated assets		Nature of SPE
	2010	2009	
	US$bn	US$bn	
Barion Funding Limited	**4.5**	4.4	Structured investment conduit
Bryant Park Funding LLC	**3.0**	3.8	Conduit
HSBC Affinity Corporation I	**4.2**	4.9	Securitisation
HSBC Auto Receivables Corporation	**–**	1.3	Securitisation
HSBC Corporate Money Fund (Euro)	**–**	0.8	Money market fund
HSBC Funding Inc V	**5.4**	5.3	Securitisation
HSBC Home Equity Loan Corporation I	**2.8**	3.1	Securitisation
HSBC Home Equity Loan Corporation II	**2.8**	3.3	Securitisation
HSBC Investor Prime Money Market Fund	**–**	10.7	Money market fund
HSBC Receivables Funding, Inc I	**3.7**	5.4	Securitisation
HSBC Receivables Inc Funding II	**2.0**	1.8	Securitisation
HSBC Sterling Liquidity Fund	**–**	7.5	Money market fund
HSBC US Dollar Liquidity Fund	**–**	23.4	Money market fund
Malachite Funding Limited	**3.9**	4.3	Structured investment conduit
Mazarin Funding Limited	**10.3**	11.3	Structured investment conduit
Metrix Funding Ltd	**1.4**	3.7	Securitisation
Metrix Securities plc	**1.0**	4.2	Securitisation
Regency Assets Limited	**6.3**	6.8	Conduit
Solitaire Funding Ltd	**13.5**	12.8	Conduit
Turquoise Receivable Trustee Ltd	**–**	0.5	Securitisation

In addition to the above, HSBC consolidates a number of individually insignificant SPEs with total assets of US$10.6bn. For further details, see 'Special purpose entities' on page 361.

In each of the above cases, HSBC has less than 50% of the voting rights, but consolidates because it has the majority of risks and rewards of ownership of the SPE, or the substance of the relationship with the SPE is such that its activities are conducted on behalf of HSBC according to its specific business needs so that HSBC obtains benefit from the SPE's operation. The consolidation of SPEs sponsored by HSBC is discussed on page 251.

Acquisitions

There were minor acquisitions and increases in investment in subsidiaries which increased goodwill by US$16m.

27 Other assets

	2010 US$m	2009 US$m
Bullion	**18,446**	13,757
Assets held for sale	**1,991**	3,118
Reinsurers' share of liabilities under insurance contracts (Note 32)	**1,865**	2,069
Endorsements and acceptances	**10,116**	9,311
Other accounts	**10,833**	16,279
	43,251	44,534

At 31 December 2010, 'Assets held for sale' included US$520m related to the sale of a majority interest in the UK-based global real estate and infrastructure private equity fund management business to the unit's senior management team. The transaction is expected to complete in the first half of 2011. Associated liabilities of US$86m are included in 'Other Liabilities'.

Non-current assets held for sale

	2010 US$m	2009 US$m
Interests in associates	**–**	105
Property, plant and equipment	**1,333**	1,639
Investment properties	**9**	1
Financial assets	**116**	1,359
Other	**3**	14
	1,461	3,118

The property, plant and equipment classified as held for sale is the result of repossession of property that had been pledged as collateral by customers. Substantially all of these assets are disposed of within 12 months of acquisition. The majority arose within the geographical segment of North America. At 31 December 2009, property, plant and equipment held for sale also included US$257m in relation to the proposed sale of 452 Fifth Avenue and 1 W. 39th Street in New York and US$370m in relation to the proposed sale of 103 Champs Elysées and 15 Rue Vernet in Paris. On completion of these transactions in 2010 gains of US$56m and US$194m respectively were recognised within 'Other operating income'.

At 31 December 2009, financial assets classified as held for sale included US$972m of vehicle finance loans and US$366m of credit card portfolios, presented in the geographical segment of North America.

Neither a gain nor loss was recognised on reclassifying assets as held for sale during the year.

28 Trading liabilities

	2010 US$m	2009 US$m
Deposits by banks	**38,678**	41,165
Customer accounts	**125,684**	99,306
Other debt securities in issue (Note 30)	**33,726**	37,592
Other liabilities – net short positions in securities	**102,615**	90,067
	300,703	268,130

At 31 December 2010, the cumulative amount of change in fair value attributable to changes in HSBC credit risk was a gain of US$142m (2009: gain of US$119m).

29 Financial liabilities designated at fair value

HSBC

	2010 US$m	2009 US$m
Deposits by banks and customer accounts	**6,527**	6,586
Liabilities to customers under investment contracts	**11,700**	10,865
Debt securities in issue (Note 30)	**46,091**	38,208
Subordinated liabilities (Note 34)	**19,395**	20,180
Preferred securities (Note 34)	**4,420**	4,253
	88,133	80,092

The carrying amount at 31 December 2010 of financial liabilities designated at fair value was US$1,631m more than the contractual amount at maturity (2009: US$1,346m more). The cumulative amount of the change in fair value attributable to changes in credit risk was a gain of US$1,279m (2009: gain of US$1,510m).

HSBC Holdings

	2010 US$m	2009 US$m
Subordinated liabilities (Note 34):		
– owed to third parties	**12,029**	12,549
– owed to HSBC undertakings	**4,259**	4,360
	16,288	16,909

The carrying amount at 31 December 2010 of financial liabilities designated at fair value was US$855m more than the contractual amount at maturity (2009: US$769m more). The cumulative amount of the change in fair value attributable to changes in credit risk was a gain of US$439m (2009: gain of US$191m).

30 Debt securities in issue

	2010 US$m	2009 US$m
Bonds and medium-term notes	**162,948**	160,295
Other debt securities in issue	**62,270**	62,401
	225,218	222,696
Of which debt securities in issue reported as:		
– trading liabilities (Note 28)	**(33,726)**	(37,592)
– financial liabilities designated at fair value (Note 29)	**(46,091)**	(38,208)
	145,401	146,896

Certain debt securities in issue are managed on a fair value basis as part of HSBC's interest rate risk management policies. The hedged portion of these debt securities is presented within the balance sheet caption 'Financial liabilities designated at fair value', with the remaining portion included within 'Trading liabilities'. The following table analyses the carrying amount of bonds and medium-term notes in issue at 31 December with original maturities greater than one year:

Notes on the Financial Statements (continued)

Bonds and medium-term notes

HSBC

	2010 US$m	2009 US$m
Fixed rate		
Secured financing:		
0.01% to 3.99%: until 2068	**6,666**	5,929
4.00% to 4.99%: until 2013	**1,956**	1,948
5.00% to 5.99%: until 2022	**387**	1,315
7.00% to 7.99%: until 2019	**209**	9
8.00% to 9.99%: until 2028	**394**	417
10.00% or higher: until 2011	**–**	43
Other fixed rate senior debt:		
0.01% to 3.99%: until 2057	**39,596**	22,554
4.00% to 4.99%: until 2046	**12,854**	15,754
5.00% to 5.99%: until 2021	**19,011**	25,619
6.00% to 6.99%: until 2033	**11,008**	11,066
7.00% to 7.99%: until 2032	**3,124**	3,900
8.00% to 9.99%: until 2036	**254**	1,737
10.00% or higher: until 2021	**337**	280
	95,796	90,571
Variable interest rate		
Secured financings – 0.01% to 13.99%: until 2068	**8,448**	13,971
FHLB advances – 0.01% to 0.99%: until 2036	**1,000**	1,000
Other variable interest rate senior debt – 0.01% to 12.99%: until 2068	**53,301**	50,258
	62,749	65,229
Structured notes		
Interest rate linked	**4**	5
Equity, equity index or credit-linked	**4,399**	4,490
	4,403	4,495
	162,948	160,295

HSBC Holdings

	2010 US$m	2009 US$m
Fixed rate senior debt, unsecured:		
4.00% to 4.99%: until 2014	**1,664**	1,791
6.00% to 6.99%: until 2024	**1,004**	1,048
	2,668	2,839

31 Other liabilities

	HSBC		HSBC Holdings	
	2010 US$m	2009 US$m	2010 US$m	2009 US$m
Amounts due to investors in funds consolidated by HSBC	**840**	48,193	**–**	–
Obligations under finance leases (Note 42)	**454**	644	**–**	–
Dividend declared and payable by HSBC Holdings (Note 11)	**1,203**	1,231	**1,203**	1,231
Endorsements and acceptances	**10,123**	9,313	**–**	–
Other liabilities	**15,430**	9,259	**29**	26
	28,050	68,640	**1,232**	1,257

32 Liabilities under insurance contracts

	Gross US$m	Reinsurers' share US$m	Net US$m
At 31 December 2010			
Non-life insurance liabilities			
Unearned premium provision	**727**	**(129)**	**598**
Notified claims	**879**	**(230)**	**649**
Claims incurred but not reported	**745**	**(75)**	**670**
Other	**105**	**2**	**107**
	2,456	**(432)**	**2,024**
Life insurance liabilities to policyholders			
Life (non-linked)	**23,583**	**(673)**	**22,910**
Investment contracts with discretionary participation features[1]	**22,074**	**–**	**22,074**
Life (linked)	**10,496**	**(760)**	**9,736**
	56,153	**(1,433)**	**54,720**
	58,609	**(1,865)**	**56,744**
At 31 December 2009			
Non-life insurance liabilities			
Unearned premium provision	833	(135)	698
Notified claims	1,032	(245)	787
Claims incurred but not reported	685	(82)	603
Other	178	(5)	173
	2,728	(467)	2,261
Life insurance liabilities to policyholders			
Life (non-linked)	20,979	(771)	20,208
Investment contracts with discretionary participation features[1]	21,014	–	21,014
Life (linked)	8,986	(831)	8,155
	50,979	(1,602)	49,377
	53,707	(2,069)	51,638

1 *Though investment contracts with discretionary participation features are financial instruments, HSBC continues to treat them as insurance contracts as permitted by IFRS 4.*

Notes on the Financial Statements (continued)

32 – Liabilities under insurance contracts

Movement on non-life insurance liabilities

	Gross US$m	Reinsurers' share US$m	Net US$m
2010			
Unearned premium reserve ('UPR')			
At 1 January	**833**	**(135)**	**698**
Changes in UPR recognised as (income)/expense	**(83)**	**(12)**	**(95)**
Gross written premiums	**1,192**	**(172)**	**1,020**
Gross earned premiums	**(1,275)**	**160**	**(1,115)**
Exchange differences and other movements	**(23)**	**18**	**(5)**
At 31 December	**727**	**(129)**	**598**
Notified and incurred but not reported claims			
At 1 January	**1,717**	**(327)**	**1,390**
Notified claims	**1,032**	**(245)**	**787**
Claims incurred but not reported	**685**	**(82)**	**603**
Claims paid in current year	**(815)**	**114**	**(701)**
Claims incurred in respect of current year	**519**	**(111)**	**408**
Claims incurred in respect of prior years	**106**	**11**	**117**
Exchange differences and other movements	**97**	**8**	**105**
At 31 December	**1,624**	**(305)**	**1,319**
Notified claims	**879**	**(230)**	**649**
Claims incurred but not reported	**745**	**(75)**	**670**
Other	**105**	**2**	**107**
Total non-life insurance liabilities	**2,456**	**(432)**	**2,024**
2009			
Unearned premium reserve ('UPR')			
At 1 January	1,136	(159)	977
Changes in UPR recognised as (income)/expense	(233)	10	(223)
Gross written premiums	1,339	(215)	1,124
Gross earned premiums	(1,572)	225	(1,347)
Exchange differences and other movements	(70)	14	(56)
At 31 December	833	(135)	698
Notified and incurred but not reported claims			
At 1 January	1,276	(271)	1,005
Notified claims	908	(230)	678
Claims incurred but not reported	368	(41)	327
Claims paid in current year	(987)	156	(831)
Claims incurred in respect of current year	939	(156)	783
Claims incurred in respect of prior years	342	(2)	340
Exchange differences and other movements	147	(54)	93
At 31 December	1,717	(327)	1,390
Notified claims	1,032	(245)	787
Claims incurred but not reported	685	(82)	603
Other	178	(5)	173
Total non-life insurance liabilities	2,728	(467)	2,261

Life insurance liabilities to policyholders

	Gross US$m	Reinsurers' share US$m	Net US$m
2010			
Life (non-linked)			
At 1 January	**20,979**	**(771)**	**20,208**
Benefits paid	**(1,355)**	**143**	**(1,212)**
Increase in liabilities to policyholders	**5,108**	**(201)**	**4,907**
Exchange differences and other movements	**(1,149)**	**156**	**(993)**
At 31 December	**23,583**	**(673)**	**22,910**
Investment contracts with discretionary participation features			
At 1 January	**21,014**	**–**	**21,014**
Benefits paid	**(2,023)**	**–**	**(2,023)**
Increase in liabilities to policyholders	**3,716**	**–**	**3,716**
Exchange differences and other movements[1]	**(633)**	**–**	**(633)**
At 31 December	**22,074**	**–**	**22,074**
Life (linked)			
At 1 January	**8,986**	**(831)**	**8,155**
Benefits paid	**(507)**	**45**	**(462)**
Increase in liabilities to policyholders	**2,520**	**99**	**2,619**
Exchange differences and other movements[2]	**(503)**	**(73)**	**(576)**
At 31 December	**10,496**	**(760)**	**9,736**
Total liabilities to policyholders	**56,153**	**(1,433)**	**54,720**
2009			
Life (non-linked)			
At 1 January	17,370	(637)	16,733
Benefits paid	(2,098)	159	(1,939)
Increase in liabilities to policyholders	4,669	(98)	4,571
Exchange differences and other movements	1,038	(195)	843
At 31 December	20,979	(771)	20,208
Investment contracts with discretionary participation features			
At 1 January	17,766	–	17,766
Benefits paid	(1,818)	–	(1,818)
Increase in liabilities to policyholders	3,934	–	3,934
Exchange differences and other movements[1]	1,132	–	1,132
At 31 December	21,014	–	21,014
Life (linked)			
At 1 January	6,067	(956)	5,111
Benefits paid	(325)	21	(304)
Increase in liabilities to policyholders	2,676	146	2,822
Exchange differences and other movements[2]	568	(42)	526
At 31 December	8,986	(831)	8,155
Total liabilities to policyholders	50,979	(1,602)	49,377

1 *Includes movement in liabilities relating to discretionary profit participation benefits due to policyholders arising from net unrealised investment gains recognised in other comprehensive income.*
2 *Includes amounts arising under reinsurance agreements.*

The increase in liabilities to policyholders represents the aggregate of all events giving rise to additional liabilities to policyholders in the year. The key factors contributing to the movement in liabilities to policyholders include death claims, surrenders, lapses, liabilities to policyholders created at the initial inception of the policies, the declaration of bonuses and other amounts attributable to policyholders.

Notes on the Financial Statements (continued)

33 – Provisions / 34 – Subordinated liabilities

33 Provisions

	2010 US$m	2009 US$m
At 1 January	1,965	1,730
Additional provisions/increase in provisions	812	894
Provisions utilised	(564)	(684)
Amounts reversed	(132)	(225)
Exchange differences and other movements	57	250
At 31 December	2,138	1,965

Provisions include US$1,257m (2009: US$1,025m) relating to legal proceedings, investigations and regulatory matters, US$405m (2009: US$449m) relating to costs arising from contingent liabilities and contractual commitments; and US$118m (2009: US$158m) relating to provisions for onerous property contracts.

34 Subordinated liabilities

HSBC

	2010 US$m	2009 US$m
Subordinated liabilities		
At amortised cost	33,387	30,478
– subordinated liabilities	28,309	23,893
– preferred securities	5,078	6,585
Designated at fair value (Note 29)	23,815	24,433
– subordinated liabilities	19,395	20,180
– preferred securities	4,420	4,253
	57,202	54,911
Subordinated liabilities		
HSBC Holdings	22,878	23,048
Other HSBC	34,324	31,863
	57,202	54,911

HSBC's subordinated liabilities

		2010 US$m	2009 US$m
Amounts owed to third parties by HSBC Holdings (see page 349)		**22,878**	23,048
Other HSBC subordinated liabilities			
US$2,939m	6.676% senior subordinated notes 2021[1]	**2,174**	–
€1,400m	5.3687% non-cumulative step-up perpetual preferred securities[2]	**1,843**	1,804
US$1,250m	4.875% subordinated notes 2020	**1,252**	–
US$1,250m	4.61% non-cumulative step-up perpetual preferred securities[2]	**1,185**	1,077
£700m	5.844% non-cumulative step-up perpetual preferred securities[3]	**1,087**	1,136
€800m	Callable subordinated floating rate notes 2016[4]	**1,070**	1,152
US$1,000m	4.625% subordinated notes 2014	**1,009**	1,002
US$1,000m	5.911% trust preferred securities 2035[5]	**994**	993
US$1,000m	5.875% subordinated notes 2034	**971**	950
€750m	5.13% non-cumulative step-up perpetual preferred securities[2]	**958**	960
£600m	4.75% subordinated notes 2046	**919**	961
US$900m	10.176% non-cumulative step-up perpetual preferred securities, series 2[2]	**891**	890
€600m	4.25% callable subordinated notes 2016[4]	**823**	904
€600m	8.03% non-cumulative step-up perpetual preferred securities[2]	**801**	862
£500m	4.75% callable subordinated notes 2020[6]	**774**	785
£500m	8.208% non-cumulative step-up perpetual preferred securities[2]	**772**	806
US$750m	Undated floating rate primary capital notes	**750**	750
US$750m	5.00% subordinated notes 2020	**747**	–
£500m	5.375% subordinated notes 2033	**729**	776
US$750m	5.625% subordinated notes 2035	**728**	712
US$700m	7.00% subordinated notes 2039	**694**	688
€500m	Callable subordinated floating rate notes 2020[7]	**592**	639
£350m	Callable subordinated variable coupon notes 2017[8]	**562**	608
£350m	5.00% callable subordinated notes 2023[9]	**547**	550
US$500m	6.00% subordinated notes 2017	**526**	521
£350m	5.375% callable subordinated step-up notes 2030[10]	**510**	531
US$500m	Undated floating rate primary capital notes	**500**	500
£300m	6.5% subordinated notes 2023	**462**	483
US$450m	Callable subordinated floating rate notes 2016[11]	**450**	449
£300m	5.862% non-cumulative step-up perpetual preferred securities[3]	**434**	412
CAD400m	4.80% subordinated notes 2022	**417**	382
US$400m	Primary capital undated floating rate notes	**407**	407
US$400m	Primary capital undated floating rate notes (second series)	**403**	404
US$400m	Primary capital undated floating rate notes (third series)	**400**	400
£225m	6.25% subordinated notes 2041	**347**	363
US$300m	7.65% subordinated notes 2025	**342**	312
US$300m	6.95% subordinated notes 2011	**310**	321
BRL500m	Subordinated certificates of deposit 2016	**301**	287
US$300m	Undated floating rate primary capital notes, series 3	**300**	300
US$300m	Callable subordinated floating rate notes 2017[12]	**300**	299
US$250m	Non-convertible subordinated obligations 2019	**248**	247
BRL383m	Subordinated certificates of deposit 2015	**231**	220
US$250m	7.20% subordinated debentures 2097	**213**	213
AUD200m	Callable subordinated floating rate notes 2016[13]	**204**	180
AUD200m	Callable subordinated floating rate notes 2020	**204**	–
US$200m	7.808% capital securities 2026	**200**	200
US$200m	8.38% capital securities 2027	**200**	200
CAD200m	4.94% subordinated debentures 2021	**200**	190
US$1,350m	9.547% non-cumulative step-up perpetual preferred securities, series 1[14]	**–**	1,349
	Other subordinated liabilities each less than US$200m	**3,343**	3,688
		34,324	31,863
		57,202	54,911

Subordinated loan capital is repayable at par on maturity, but some is repayable prior to maturity at the option of the borrower, generally subject to prior notification to the Financial Services Authority and, where relevant, the consent of the local banking regulator, and in certain cases at a premium over par. Interest rates on the floating rate loan capital are related to interbank offered rates. On the remaining subordinated loan capital, interest is payable at fixed rates of up to 10.176%.

Notes on the Financial Statements (continued)

1 *Approximately 25% of the 6.676% senior subordinated notes 2021 is held by HSBC Holdings.*
2 *See 'Step-up perpetual preferred securities' below, note (a) 'Guaranteed by HSBC Holdings'.*
3 *See 'Step-up perpetual preferred securities' below, note (b) 'Guaranteed by HSBC Bank'.*
4 *On 15 February 2011, HSBC gave notice to holders of its €800m callable subordinated floating rate notes 2016 and its €600m 4.25% callable subordinated notes 2016 that it will call and redeem the notes at par on 29 March 2011 and 18 March 2011, respectively.*
5 *The distributions on the trust preferred securities change in November 2015 to three-month dollar LIBOR plus 1.926%.*
6 *The interest rate on the 4.75% callable subordinated notes 2020 changes in September 2015 to three-month sterling LIBOR plus 0.82%.*
7 *The interest margin on the callable subordinated floating rate notes 2020 increases by 0.5% from September 2015.*
8 *The interest rate on the callable subordinated variable coupon notes 2017 is fixed at 5.75% until June 2012. Thereafter, the rate per annum is the sum of the gross redemption yield of the then prevailing five-year UK gilt plus 1.70%.*
9 *The interest rate on the 5.00% callable subordinated notes 2023 changes in March 2018 to become the rate per annum which is the sum of the gross redemption yield of the then prevailing five-year UK gilt plus 1.80%.*
10 *The interest rate on the 5.375% callable subordinated step-up notes 2030 changes in November 2025 to three-month sterling LIBOR plus 1.50%.*
11 *The interest margin on the US$450m callable subordinated floating rate notes 2016 increases by 0.5% from July 2011.*
12 *The interest margin on the callable subordinated floating rate notes 2017 increases by 0.5% from July 2012.*
13 *The interest margin on the callable subordinated floating rate notes 2016 increases by 0.5% from May 2011.*
14 *In June 2010, HSBC redeemed its 9.547% non-cumulative step-up preferred securities, series 1 at par.*

Footnotes 4 to 13 relate to notes that are repayable at the option of the borrower on the date of the change of the interest rate, and at subsequent interest rate reset dates and interest payment dates in some cases, subject to prior notification to the Financial Services Authority and, where relevant, the consent of the local banking regulator.

Step-up perpetual preferred securities

(a) Guaranteed by HSBC Holdings

The six issues of non-cumulative step-up perpetual preferred securities (footnote 2) were made by Jersey limited partnerships and are guaranteed, on a subordinated basis, by HSBC Holdings. The proceeds of the issues were on-lent to HSBC Holdings by the limited partnerships by issue of subordinated notes. The preferred securities qualify as tier 1 hybrid capital for HSBC. The preferred securities, together with the guarantee, are intended to provide investors with rights to income and capital distributions and distributions upon liquidation of HSBC Holdings that are equivalent to the rights that they would have had if they had purchased non-cumulative perpetual preference shares of HSBC Holdings.

The preferred securities are perpetual, but redeemable in 2014, 2013, 2016, 2030, 2012 and 2015, respectively, at the option of the general partner of the limited partnerships. If not redeemed, the distributions payable step-up and become floating rate or, for the sterling issue, for each successive five-year period the sum of the then five-year benchmark UK gilt plus a margin. There are limitations on the payment of distributions if prohibited under UK banking regulations or other requirements, if a payment would cause a breach of HSBC's capital adequacy requirements, or if HSBC Holdings has insufficient distributable reserves (as defined).

HSBC Holdings has covenanted that if it is prevented under certain circumstances from paying distributions on the preferred securities in full, it will not pay dividends or other distributions in respect of its ordinary shares, or effect repurchase or redemption of its ordinary shares, until after a distribution has been paid in full.

If (i) HSBC's total capital ratio falls below the regulatory minimum ratio required, or (ii) the Directors expect that, in view of the deteriorating financial condition of HSBC Holdings, the former will occur in the near term, then the preferred securities will be substituted by preference shares of HSBC Holdings having economic terms which are in all material respects equivalent to those of the preferred securities and the guarantee taken together.

(b) Guaranteed by HSBC Bank

The two issues of non-cumulative step-up perpetual preferred securities (footnote 3) were made by Jersey limited partnerships and are guaranteed, on a subordinated basis, by HSBC Bank. The proceeds of the issues were on-lent to HSBC Bank by the limited partnerships by issue of subordinated notes. The preferred securities qualify as tier 1 hybrid capital for HSBC and for HSBC Bank on a solo and consolidated basis and, together with the guarantee, are intended to provide investors with rights to income and capital distributions and distributions upon liquidation of HSBC Bank that are equivalent to the rights they would have had if they had purchased non-cumulative perpetual preference shares of HSBC Bank.

The two issues of preferred securities are perpetual, but redeemable in 2031 and 2020, respectively, at the option of the general partner of the limited partnerships. If not redeemed, the distributions payable step-up and become floating rate. The same limitations on the payment of distributions apply to HSBC Bank as to HSBC Holdings, as described above. HSBC Bank has provided a similar covenant to that provided by HSBC Holdings, also as described above.

If (i) any of the two issues of preferred securities are outstanding in November 2048 or April 2049, respectively, or (ii) the total capital ratio of HSBC Bank on a solo and consolidated basis falls below the regulatory minimum ratio required, or (iii) in view of the deteriorating financial condition of HSBC Bank, the Directors expect (ii) to occur in the near term, then the preferred securities will be substituted by preference shares of HSBC Bank having economic terms which are in all material respects equivalent to those of the preferred securities and the guarantee taken together.

HSBC Holdings

	2010 US$m	2009 US$m
Subordinated liabilities:		
– at amortised cost	13,313	14,406
– designated at fair value (Note 29)	16,288	16,909
	29,601	31,315

HSBC Holdings' subordinated liabilities

		2010 US$m	2009 US$m
Amounts owed to third parties			
US$2,500m	6.5% subordinated notes 2037	2,695	2,659
€1,750m	6.0% subordinated notes 2019	2,578	2,835
€1,600m	6.25% subordinated notes 2018	2,142	2,306
US$2,000m	6.5% subordinated notes 2036	2,050	2,052
£900m	6.375% callable subordinated notes 2022[1]	1,493	1,517
US$1,400m	5.25% subordinated notes 2012	1,492	1,488
US$1,500m	6.8% subordinated notes 2038	1,485	1,484
€1,000m	5.375% subordinated notes 2012	1,405	1,549
£900m	6.0% subordinated notes 2040	1,372	–
£750m	7.0% subordinated notes 2038	1,210	1,267
£650m	6.75% subordinated notes 2028	1,000	1,043
£650m	5.75% subordinated notes 2027	971	1,000
€700m	3.625% callable subordinated notes 2020[2]	928	1,005
US$750m	Callable subordinated floating rate notes 2016[3]	750	750
US$488m	7.625% subordinated notes 2032	582	587
£250m	9.875% subordinated bonds 2018[4]	467	496
US$222m	7.35% subordinated notes 2032	258	260
US$750m	Callable subordinated floating rate notes 2015[5]	–	750
		22,878	23,048
Amounts owed to HSBC undertakings			
€1,400m	5.3687% fixed/floating subordinated notes 2043 – HSBC Capital Funding (Euro 2) LP	1,957	2,042
US$1,250m	4.61% fixed/floating subordinated notes 2043 – HSBC Capital Funding (Dollar 2) LP	1,274	1,223
€750m	5.13% fixed/floating subordinated notes 2044 – HSBC Capital Funding (Euro 3) LP	1,028	1,095
US$900m	10.176% subordinated step-up cumulative notes 2040 – HSBC Capital Funding (Dollar 1) LP	891	890
€600m	8.03% subordinated step-up cumulative notes 2040 – HSBC Capital Funding (Euro 1) LP	801	862
£500m	8.208% subordinated step-up cumulative notes 2040 – HSBC Capital Funding (Sterling 1) LP	772	806
US$1,350m	9.547% subordinated step-up cumulative notes 2040 – HSBC Capital Funding (Dollar 1) LP[6]	–	1,349
		6,723	8,267
		29,601	31,315

1 *The interest rate on the 6.375% callable subordinated notes 2022 changes in October 2017 to become three-month sterling LIBOR plus 1.3%. The notes may be redeemed at par from October 2017 at the option of the borrower, subject to the prior notification to the FSA.*

Notes on the Financial Statements (continued)

2 *The interest rate on the 3.625% callable subordinated notes 2020 changes in June 2015 to become three-month EURIBOR plus 0.93%. The notes may be redeemed at par from June 2015 at the option of the borrower, subject to the prior notification to the FSA.*
3 *The interest margin on the callable subordinated floating rate notes 2016 increases by 0.5% from October 2011. The notes are repayable from their step up date at the option of the borrower, subject to the prior notification to the FSA.*
4 *The interest rate on the 9.875% subordinated bonds 2018 changes in April 2013 to become the higher of (i) 9.875% or (ii) the sum of the yield on the relevant benchmark treasury stock plus 2.5%. The bonds may be redeemed in April 2013 at par and redemption has also been allowed from April 1998, subject to the prior notification to the FSA, for an amount based on the redemption yields of the relevant benchmark treasury stocks.*
5 *In March 2010, HSBC Holdings redeemed its US$750m callable subordinated floating rate notes due 2015 at par.*
6 *In June 2010, HSBC Holdings redeemed its 9.547% subordinated step-up cumulative notes 2040 – HSBC Capital Funding (Dollar 1) LP at par.*

35 Maturity analysis of assets and liabilities

The following is an analysis, by remaining contractual maturities at the balance sheet date, of asset and liability line items that represent amounts expected to be recovered or settled within one year, and after more than one year.

Trading assets and liabilities are excluded because they are not held for collection or settlement over the period of contractual maturity.

Maturity analysis of assets and liabilities

HSBC

	At 31 December 2010			At 31 December 2009		
	Due within one year US$m	**Due after more than one year US$m**	**Total US$m**	Due within one year US$m	Due after more than one year US$m	Total US$m
Assets						
Financial assets designated at fair value	**3,030**	**33,981**	**37,011**	3,786	33,395	37,181
Loans and advances to banks	**200,098**	**8,173**	**208,271**	172,916	6,865	179,781
Loans and advances to customers	**424,713**	**533,653**	**958,366**	381,967	514,264	896,231
Financial investments	**149,954**	**250,801**	**400,755**	134,824	234,334	369,158
Other financial assets	**19,417**	**5,519**	**24,936**	26,189	7,383	33,572
	797,212	**832,127**	**1,629,339**	719,682	796,241	1,515,923
Liabilities						
Deposits by banks	**105,462**	**5,122**	**110,584**	118,308	6,564	124,872
Customer accounts	**1,181,095**	**46,630**	**1,227,725**	1,114,149	44,885	1,159,034
Financial liabilities designated at fair value	**10,141**	**77,992**	**88,133**	4,666	75,426	80,092
Debt securities in issue	**86,096**	**59,305**	**145,401**	83,590	63,306	146,896
Other financial liabilities	**24,865**	**4,792**	**29,657**	67,061	3,606	70,667
Subordinated liabilities	**791**	**32,596**	**33,387**	369	30,109	30,478
	1,408,450	**226,437**	**1,634,887**	1,388,143	223,896	1,612,039

HSBC Holdings

	At 31 December 2010			At 31 December 2009		
	Due within one year US$m	**Due after more than one year US$m**	**Total US$m**	Due within one year US$m	Due after more than one year US$m	Total US$m
Assets						
Loans and advances to HSBC undertakings	**13,691**	**7,547**	**21,238**	18,067	5,145	23,212
Financial investments	**–**	**2,025**	**2,025**	–	2,455	2,455
Other financial assets	**1**	**–**	**1**	4	–	4
	13,692	**9,572**	**23,264**	18,071	7,600	25,671
Liabilities						
Amounts owed to HSBC undertakings	**1,480**	**1,452**	**2,932**	277	3,434	3,711
Financial liabilities designated at fair value	**–**	**16,288**	**16,288**	–	16,909	16,909
Debt securities in issue	**–**	**2,668**	**2,668**	–	2,839	2,839
Other financial liabilities	**1,782**	**–**	**1,782**	1,240	17	1,257
Subordinated liabilities	**–**	**13,313**	**13,313**	–	14,406	14,406
	3,262	**33,721**	**36,983**	1,517	37,605	39,122

36 Foreign exchange exposures

Structural foreign exchange exposures

HSBC's structural foreign exchange exposures are represented by the net asset value of its foreign exchange equity and subordinated debt investments in subsidiaries, branches, joint ventures and associates with non-US dollar functional currencies. Gains or losses on structural foreign exchange exposures are recognised in other comprehensive income. HSBC's management of its structural foreign exchange exposures is discussed in the 'Report of the Directors: Risk' on page 149.

In its separate financial statements, HSBC Holdings recognises its foreign exchange gains and losses on structural foreign exchange exposures in the income statement.

Net structural foreign exchange exposures

	2010 US$m	2009 US$m
Currency of structural exposure		
Pound sterling	**23,247**	21,369
Euro	**23,222**	25,284
Chinese renminbi	**17,454**	13,398
Brazilian reais	**6,004**	5,234
Mexican pesos	**5,991**	5,393
Indian rupees	**4,754**	3,836
Canadian dollars	**4,012**	3,620
Swiss francs	**3,357**	2,910
Hong Kong dollars	**2,659**	3,842
UAE dirhams	**2,469**	2,209
Turkish lira	**1,854**	1,741
Malaysian ringgit	**1,619**	1,300
Korean won	**1,456**	1,412
Taiwanese dollars	**1,429**	547
Australian dollars	**1,381**	1,017
Indonesian rupiah	**1,190**	1,057
Saudi riyals	**907**	657
Argentine pesos	**881**	675
Egyptian pounds	**642**	561
Philippine pesos	**635**	473
Vietnamese dong	**621**	505
Singapore dollars	**596**	556
Qatari rial	**510**	384
Thai baht	**424**	357
Costa Rican colon	**416**	375
Honduran lempira	**291**	282
Japanese yen	**267**	228
Colombian pesos	**266**	220
Russian rouble	**257**	295
Chilean pesos	**249**	230
South African rand	**238**	201
Omani rial	**234**	210
Brunei dollars	**227**	132
Jordanian dinar	**181**	159
New Zealand dollars	**172**	161
Algerian dinar	**155**	146
Sri Lankan rupee	**136**	141
Bahraini dinar	**133**	85
Kazakh tenge	**109**	64
Others, each less than US$100m	**658**	523
Total	**111,303**	101,789

Shareholders' equity would decrease by US$2,213m (2009: US$2,222m) if euro and sterling foreign currency exchange rates weakened by 5% relative to the US dollar.

37 Assets charged as security for liabilities and collateral accepted as security for assets

Financial assets pledged to secure liabilities

	Assets pledged at 31 December	
	2010	2009
	US$m	US$m
Treasury bills and other eligible securities	**5,859**	3,970
Loans and advances to banks	**11,773**	6,767
Loans and advances to customers	**60,500**	77,699
Debt securities	**214,126**	203,766
Equity shares	**7,216**	7,305
Other	**931**	646
	300,405	300,153

These transactions are conducted under terms that are usual and customary to collateralised transactions, including, where relevant, standard securities lending and repurchase agreements.

Collateral accepted as security for assets

The fair value of assets accepted as collateral that HSBC is permitted to sell or repledge in the absence of default is US$333,921m (2009: US$362,560m). The fair value of any such collateral that has been sold or repledged was US$205,470m (2009: US$215,940m). HSBC is obliged to return equivalent securities.

These transactions are conducted under terms that are usual and customary to standard securities borrowing and reverse repurchase agreements.

38 Non-controlling interests

	2010	2009
	US$m	US$m
Non-controlling interests attributable to holders of ordinary shares in subsidiaries	**4,522**	4,665
Preference shares issued by subsidiaries	**2,726**	2,697
	7,248	7,362

Preference shares issued by subsidiaries

		2010	2009
		US$m	US$m
US$575m	6.36% non-cumulative preferred stock, Series B[1]	**559**	559
US$518m	Floating rate non-cumulative preferred stock, Series F[2]	**518**	518
US$374m	Floating rate non-cumulative preferred stock, Series G[3]	**374**	374
US$374m	6.50% non-cumulative preferred stock, Series H[3]	**374**	374
CAD250m	Non-cumulative 5 year rate reset class 1 preferred shares, Series E[4]	**251**	238
CAD175m	Non-cumulative redeemable class 1 preferred shares, Series C[5]	**175**	167
CAD175m	Non-cumulative class 1 preferred shares, Series D[5]	**175**	167
US$150m	Depositary shares each representing 25% interest in a share of adjustable-rate cumulative preferred stock, Series D[6]	**150**	150
US$150m	Cumulative preferred stock[7]	**150**	150
		2,726	2,697

1 *The Series B preferred stock has been redeemable at the option of HSBC Finance Corporation, in whole or in part, from 24 June 2010 at par.*
2 *The Series F preferred stock has been redeemable at par at the option of HSBC USA, Inc., in whole or in part, on any dividend payment date from 7 April 2010.*
3 *The Series G and Series H preferred stock are redeemable at par at the option of HSBC USA, Inc., in whole or in part, at any time from 1 January 2011 and 1 July 2011, respectively.*
4 *The Series E preferred shares are redeemable at par at the option of HSBC Bank Canada, in whole or in part commencing 30 June 2014 and on 30 June every five years thereafter.*
5 *The Series C and Series D preferred shares have been redeemable at a declining premium above par at the option of HSBC Bank Canada, in whole or in part, from 30 June 2010 and 31 December 2010, respectively.*
6 *The preferred stock has been redeemable at the option of HSBC USA, Inc., in whole or in part, from 1 July 1999 at par.*
7 *The preferred stock has been redeemable at the option of HSBC USA, Inc., in whole or in part, from 1 October 2007 at par.*

All redemptions are subject to prior notification to the Financial Services Authority and, where relevant, the local banking regulator.

39 Called up share capital and other equity instruments

Issued and fully paid

	2010 US$m	2009 US$m
HSBC Holdings ordinary shares[1]	**8,843**	8,705

	Number	US$m
HSBC Holdings ordinary shares of US$0.50 each		
At 1 January 2010	**17,408,206,768**	**8,705**
Shares issued under HSBC employee share plans	**25,001,734**	**12**
Shares issued in lieu of dividends	**252,947,400**	**126**
At 31 December 2010	**17,686,155,902**	**8,843**
At 1 January 2009	12,105,265,082	6,053
Shares issued under HSBC employee share plans	7,476,952	4
Shares issued in lieu of dividends	235,225,669	118
Shares issued in respect of rights issue	5,060,239,065	2,530
At 31 December 2009	17,408,206,768	8,705

1 *All ordinary shares in issue confer identical rights in respect of capital, dividends, voting and otherwise.*

	Number	US$m
HSBC Holdings non-cumulative preference shares of US$0.01 each		
At 1 January 2010 and 31 December 2010	**1,450,000**	**–**
At 1 January 2009 and 31 December 2009	1,450,000	–

Dividends on the HSBC Holdings non-cumulative dollar preference shares ('Dollar Preference Shares') in issue are paid quarterly at the sole and absolute discretion of the Board of Directors. The Board of Directors will not declare a dividend on the Dollar Preference Shares in issue if payment of the dividend would cause HSBC Holdings not to meet the applicable capital adequacy requirements of the FSA or the profit of HSBC Holdings available for distribution as dividends is not sufficient to enable HSBC Holdings to pay in full both dividends on the Dollar Preference Shares in issue and dividends on any other shares that are scheduled to be paid on the same date and that have an equal right to dividends. HSBC Holdings may not declare or pay dividends on any class of its shares ranking lower in the right to dividends than the Dollar Preference Shares in issue nor redeem nor purchase in any manner any of its other shares ranking equal with or lower than the Dollar Preference Shares in issue unless it has paid in full, or set aside an amount to provide for payment in full, the dividends on the Dollar Preference Shares in issue for the then-current dividend period. The Dollar Preference Shares in issue carry no rights to conversion into ordinary shares of HSBC Holdings. Holders of the Dollar Preference Shares in issue will only be entitled to attend and vote at general meetings of shareholders of HSBC Holdings if the dividend payable on the Dollar Preference Shares in issue has not been paid in full for four consecutive dividend payment dates. In such circumstances, holders of the Dollar Preference Shares in issue will be entitled to vote on all matters put to general meetings until such time as HSBC Holdings has paid a full dividend on the Dollar Preference Shares in issue. HSBC Holdings may redeem the Dollar Preference Shares in issue in whole at any time on or after 16 December 2010, subject to prior notification to the FSA.

HSBC Holdings non-cumulative preference shares of £0.01 each

On 29 December 2010 HSBC Holdings issued one non-cumulative sterling preference share of £0.01 ('Sterling Preference Share') to facilitate the cancellation of the non-voting deferred shares and comply with the provisions of the Companies (Authorised Minimum) Regulations 2009. Dividends on the Sterling Preference Share in issue are paid quarterly at the sole and absolute discretion of the Board. The Sterling Preference Share in issue carries no rights to conversion into ordinary shares of HSBC Holdings and no rights to attend and vote at general meetings of shareholders of HSBC Holdings. HSBC Holdings may redeem the Sterling Preference Share in issue in whole at any time at the option of the Company.

Notes on the Financial Statements (continued)

HSBC Holdings non-voting deferred shares

301,500 non-voting deferred shares of £1 each were in issue throughout 2009 and up to 29 December 2010 and were held by a subsidiary of HSBC Holdings. As part of a technical internal capital reorganisation necessitated by the amended EU Capital Requirements Directive 2, which applied to HSBC Holdings from 31 December 2010, all of the non-voting deferred shares of £1 each were cancelled.

Other equity instruments

On 9 April 2008, HSBC Holdings issued, in bearer form, 88m 8.125% Perpetual Subordinated Capital Securities ('Capital Securities'), each with a par value of US$25 and with an aggregate nominal value of US$2,200m. The Capital Securities were issued at par value, raising US$2,133m, net of issuance costs. The Capital Securities were issued to support the development of and to strengthen further HSBC's capital base. Coupon payments on the Capital Securities are paid quarterly in arrears from 15 July 2008 and may be deferred at the discretion of HSBC Holdings. The Capital Securities have no fixed maturity and are redeemable at HSBC's option on or after 15 April 2013 at their principal amounts together with any accrued, unpaid and deferred coupon payments. While any coupon payments are unpaid or deferred, HSBC Holdings will not declare, pay dividends or make distributions or similar periodic payments in respect of, or repurchase, redeem or otherwise acquire any securities of lower or equal rank. At the Company's discretion, and subject to certain conditions being satisfied, the Capital Securities may be exchanged on any coupon payment date for non-cumulative preference shares to be issued by HSBC Holdings and which would rank *pari passu* with the dollar and sterling preference shares in issue. The preference shares will be issued at a nominal value of US$0.01 per share and a premium of US$24.99 per share, with both such amounts being subscribed and fully paid.

During June 2010, HSBC Holdings issued, in bearer form, 152m 8.00% of Perpetual Subordinated Capital Securities, Series 2 ('Capital Securities, Series 2'), each with a par value of US$25 and with an aggregate nominal value of US$3,800m. The Capital Securities, Series 2 were issued at par value, raising US$3,718m, net of issuance costs. These securities were issued on substantially the same terms as the Capital Securities issued in 2008. Coupon payments on the Capital Securities, Series 2 are paid quarterly in arrears from 15 September 2010 and may be deferred at the discretion of HSBC Holdings. The Capital Securities, Series 2 have no fixed maturity and are redeemable at HSBC's option on or after 15 December 2015 at their principal amounts together with any accrued, unpaid and deferred coupon payments. At the Company's discretion, and subject to certain conditions being satisfied, the Capital Securities, Series 2 may be exchanged on any coupon payment date for non-cumulative preference shares to be issued by HSBC Holdings and which would rank *pari passu* with the dollar and sterling preference shares in issue. The preference shares will be issued at a nominal value of US$0.01 per share and a premium of US$24.99 per share, with both such amounts being subscribed and fully paid.

Shares under option

Details of the options outstanding to subscribe for HSBC Holdings ordinary shares under the HSBC Holdings Group Share Option Plan, HSBC Holdings Executive Share Option Scheme, the HSBC Share Plan and HSBC Holdings savings-related share option plans are given in Note 9.

Aggregate options outstanding under these plans

	Number of HSBC Holdings ordinary shares	Period of exercise	Exercise price
31 December 2010	**249,242,968**	**2011 to 2016**	**£3.3116 – 8.4024**
	47,428,892	**2011 to 2016**	**HK$37.8797 – 94.5057**
	3,128,508	**2011 to 2016**	**€3.6361 – 9.5912**
	10,899,415	**2011 to 2016**	**US$4.8876 – 12.0958**
31 December 2009[1]	270,742,989	2010 to 2015	£3.3116 – 8.4024
	50,938,242	2010 to 2015	HK$37.8797 – 94.5057
	3,283,710	2010 to 2015	€3.6361 – 9.5912
	12,073,216	2010 to 2015	US$4.8876 – 12.0958
31 December 2008	211,226,573	2009 to 2015	£5.3496 – 9.642
	11,344,167	2009 to 2014	HK$103.4401 – 108.4483
	1,304,119	2009 to 2014	€8.6720 – 11.0062
	7,382,145	2009 to 2014	US$13.3290 – 14.7478

1 *During 2009, the number and prices of unexercised share options were adjusted for the rights issue.*

HSBC France and subsidiary company plans

Following the acquisition of HSBC France in 2000, outstanding employee share options over HSBC France shares vested. On exercise of the options, the HSBC France shares were exchangeable for HSBC Holdings ordinary shares at the ratio of 14.917916 HSBC Holdings ordinary shares for each HSBC France.

During 2010, no employee share options (2009: nil) were exercised and no HSBC France shares were issued and exchanged for HSBC Holdings ordinary shares (2009: nil). During 2010, 604,250 options over HSBC France shares lapsed (2009: 183,627). At 31 December 2010, there are no employee share options outstanding and the HSBC Holdings Employee Benefit Trust 2001 (No. 1) held no (2009: 9,963,718) HSBC Holdings ordinary shares to exchange for HSBC France shares arising from the exercise of options.

HSBC France options effectively outstanding over HSBC Holdings ordinary shares

	Number of HSBC France shares exchangeable for HSBC Holdings ordinary shares	Period of exercise	Exercise price
31 December 2010	**–**	**–**	**–**
31 December 2009	604,250	2010	€142.50
31 December 2008	787,877	2009 to 2010	€81.71 – 142.50

HSBC Private Bank France plan

There are also outstanding options over the shares of HSBC Private Bank France, a subsidiary of HSBC France.

On exercise of the options, the HSBC Private Bank France shares are exchangeable for HSBC Holdings ordinary shares at the ratio of 2.099984 HSBC Holdings ordinary shares for each HSBC Private Bank France share. During 2010, 4,420 (2009: 33,456) HSBC Private Bank France shares were issued following the exercise of employee share options and exchanged for 9,281 (2009: 70,248) HSBC Holdings ordinary shares, such shares being delivered from The CCF Employee Benefit Trust 2001 (Private Banking France). During 2010, no options over HSBC Private Bank France shares lapsed (2009: 9,000). At 31 December 2010, The CCF Employee Benefit Trust 2001 (Private Banking France) held 989,502 (2009: 998,783) HSBC Holdings ordinary shares which may be exchanged for HSBC Private Bank France shares arising from the exercise of options.

HSBC Private Bank France options effectively outstanding over HSBC Holdings ordinary shares

	Number of HSBC Private Bank France shares exchangeable for HSBC Holdings ordinary shares	Period of exercise	Exercise price
31 December 2010	**287,100**	**2011 to 2012**	**€20.80 – 22.22**
31 December 2009	291,520	2010 to 2012	€12.44 – 22.22
31 December 2008	333,976	2009 to 2012	€10.84 – 22.22

HSBC Finance plan

Following the acquisition of HSBC Finance in 2003, all outstanding options and equity-based awards over HSBC Finance common shares were converted into rights to receive HSBC Holdings ordinary shares in the same ratio as the share exchange offer for HSBC Finance (2.675 HSBC Holdings ordinary shares for each HSBC Finance common share) and the exercise prices per share adjusted accordingly. During 2010, 306,964 options (2009: 20,000) over HSBC Holdings ordinary shares were exercised and 306,964 (2009: 20,000) HSBC Holdings ordinary shares delivered from The HSBC (Household) Employee Benefit Trust 2003 to satisfy the exercise of these options. During 2010, options over 6,681,169 (2009: 5,606,714) HSBC Holdings ordinary shares lapsed. At 31 December 2010, the Trust held a total of 2,335,315 (2009: 2,642,279) HSBC Holdings ordinary shares and 1,455 (2009: 1,455) ADSs, which may be used to satisfy the exercise of these options and equity-based awards under the HSBC Finance share plans. Each ADS represents five HSBC Holdings ordinary shares.

Options outstanding over HSBC Holdings ordinary shares under the HSBC Finance share plan

	Number of HSBC Holdings ordinary shares	Period of exercise	Exercise price
31 December 2010	**11,117,826**	**2011 to 2012**	**US$9.29 – 18.62**
31 December 2009[1]	18,105,959	2010 to 2012	US$9.29 – 18.62
31 December 2008	20,681,582	2009 to 2012	US$10.66 – 21.37

1 *During 2009, the number and prices of unexercised share options were adjusted for the rights issue.*

HSBC Bank Bermuda plans

Following the acquisition of HSBC Bank Bermuda in 2004, all outstanding employee share options over HSBC Bank Bermuda shares were converted into rights to receive HSBC Holdings ordinary shares based on the consideration of US$40 for each HSBC Bank Bermuda share and the average closing price of HSBC Holdings ordinary shares, derived from the London Stock Exchange Daily Official List, for the five business days preceding the closing date of the acquisition. During 2010, options over 4,781 HSBC Holdings ordinary shares were exercised (2009: 18,153) and satisfied by delivery from the HSBC (Bank of Bermuda) Employee Benefit Trust 2004. During 2010, options over 137,888 (2009: 24,673) HSBC Holdings ordinary shares lapsed. At 31 December 2010, the HSBC (Bank of Bermuda) Employee Benefit Trust 2004 held 2,108,830 (2009: 2,113,611) HSBC Holdings ordinary shares which may be used to satisfy the exercise of options.

Options outstanding over HSBC Holdings ordinary shares under the HSBC Bank Bermuda share plan

	Number of HSBC Holdings ordinary shares	Period of exercise	Exercise price
31 December 2010	**2,339,033**	**2011 to 2013**	**US$9.32 – 15.99**
31 December 2009[1]	2,481,702	2010 to 2013	US$6.13 – 15.99
31 December 2008	2,205,321	2009 to 2013	US$7.04 – 18.35

1 *During 2009, the number and prices of unexercised share options were adjusted for the rights issue.*

Maximum obligation to deliver HSBC Holdings ordinary shares

At 31 December 2010, the maximum obligation to deliver HSBC Holdings ordinary shares under all of the above option arrangements, together with awards of Performance Shares and Restricted Shares under the HSBC Share Plan, was 558,187,326 (2009: 559,960,290). The total number of shares at 31 December 2010 held by employee benefit trusts that may be used to satisfy such obligations to deliver HSBC Holdings ordinary shares was 79,541,700 (2009: 134,903,061).

40 Notes on the statement of cash flows

Non-cash items included in profit before tax

	HSBC			HSBC Holdings	
	2010 US$m	2009 US$m	2008 US$m	**2010 US$m**	2009 US$m
Depreciation, amortisation and impairment	**2,801**	2,538	13,367	**2**	5,947
Gains arising from dilution of interests in associates	**(188)**	–	–	**–**	–
Revaluations on investment property	**(93)**	24	92	**–**	–
Share-based payment expense	**812**	683	819	**28**	21
Loan impairment losses gross of recoveries and other credit risk provisions	**15,059**	27,378	25,771	**–**	–
Provisions	**680**	669	591	**–**	–
Impairment of financial investments	**105**	358	1,042	**113**	–
Charge for defined benefit plans	**526**	192	490	**–**	–
Accretion of discounts and amortisation of premiums	**(815)**	(458)	(867)	**42**	6
	18,887	31,384	41,305	**185**	5,974

Change in operating assets

	HSBC			HSBC Holdings	
	2010 US$m	2009 US$m	2008 US$m	**2010 US$m**	2009 US$m
Change in loans to HSBC undertakings	**–**	–	–	**1,974**	(11,408)
Change in prepayments and accrued income	**457**	3,198	4,178	**(5)**	(44)
Change in net trading securities and net derivatives	**60,337**	15,388	(23,293)	**1,119**	354
Change in loans and advances to banks	**5,213**	(30,354)	22,596	**–**	–
Change in loans and advances to customers	**(79,283)**	6,149	7,279	**–**	–
Change in financial assets designated at fair value	**154**	(8,911)	12,757	**–**	–
Change in other assets	**(145)**	(6,273)	(5,394)	**3**	21
	(13,267)	(20,803)	18,123	**3,091**	(11,077)

Change in operating liabilities

	HSBC			HSBC Holdings	
	2010 US$m	2009 US$m	2008 US$m	**2010 US$m**	2009 US$m
Change in accruals and deferred income	**716**	(2,258)	(6,169)	**147**	131
Change in deposits by banks	**(14,288)**	(5,216)	(3,038)	**–**	–
Change in customer accounts	**68,691**	41,983	32,372	**–**	–
Change in debt securities in issue	**(1,495)**	(32,797)	(67,152)	**(171)**	21
Change in financial liabilities designated at fair value	**5,659**	7,430	(15,352)	**(621)**	2,411
Change in other liabilities	**(17,011)**	5,503	(4,074)	**(1,109)**	(523)
	42,272	14,645	(63,413)	**(1,754)**	2,040

Cash and cash equivalents

	HSBC			HSBC Holdings	
	2010 US$m	2009 US$m	2008 US$m	**2010 US$m**	2009 US$m
Cash at bank with HSBC undertakings		–	–	**459**	224
Cash and balances at central banks	**57,383**	60,655	52,396	**–**	–
Items in the course of collection from other banks	**6,072**	6,395	6,003	**–**	–
Loans and advances to banks of one month or less	**189,197**	160,673	165,066	**–**	–
Treasury bills, other bills and certificates of deposit less than three months	**28,087**	28,777	62,639	**–**	–
Less: items in the course of transmission to other banks	**(6,663)**	(5,734)	(7,232)	**–**	–
	274,076	250,766	278,872	**459**	224

Interest and dividends

	HSBC			HSBC Holdings	
	2010 US$m	2009 US$m	2008 US$m	**2010 US$m**	2009 US$m
Interest paid	**(21,405)**	(29,030)	(60,342)	**(2,363)**	(2,513)
Interest received	**63,696**	74,062	107,019	**1,405**	1,560
Dividends received	**563**	1,023	1,876	**7,008**	7,488

The amount of cash and cash equivalents not available for use by HSBC at 31 December 2010 was US$37,413m (2009: US$19,119m), of which US$28,780m (2009: US$11,595m) related to mandatory deposits at central banks.

41 Contingent liabilities, contractual commitments and guarantees

	HSBC		HSBC Holdings	
	2010	2009	**2010**	2009
	US$m	US$m	**US$m**	US$m
Guarantees and contingent liabilities				
Guarantees and irrevocable letters of credit pledged as collateral security	**71,157**	73,385	**46,988**	35,073
Other contingent liabilities	**166**	174	**–**	–
	71,323	73,559	**46,988**	35,073
Commitments				
Documentary credits and short-term trade-related transactions	**12,051**	9,066	**–**	–
Forward asset purchases and forward forward deposits placed	**30**	192	**–**	–
Undrawn formal standby facilities, credit lines and other commitments to lend	**590,432**	548,792	**2,720**	3,240
	602,513	558,050	**2,720**	3,240

The above table discloses the nominal principal amounts of commitments excluding capital commitments, which are separately disclosed below, guarantees and other contingent liabilities; mainly credit-related instruments including both financial and non-financial guarantees and commitments to extend credit. Contingent liabilities arising from legal proceedings and regulatory matters against the Group are disclosed in Note 44. Nominal principal amounts represent the amounts at risk should contracts be fully drawn upon and clients default. The amount of the loan commitments shown above reflects, where relevant, the expected level of take-up of pre-approved loan offers made by mailshots to personal customers. As a significant portion of guarantees and commitments is expected to expire without being drawn upon, the total of the nominal principal amounts is not representative of future liquidity requirements.

Guarantees

HSBC provides guarantees and similar undertakings on behalf of both third-party customers and other entities within the HSBC Group. These guarantees are generally provided in the normal course of HSBC's banking business. The principal types of guarantees provided, and the maximum potential amount of future payments which HSBC could be required to make at 31 December 2010, were as follows:

	At 31 December 2010		At 31 December 2009	
	Guarantees in favour of third parties	**Guarantees by HSBC Holdings in favour of other HSBC Group entities**	Guarantees in favour of third parties	Guarantees by HSBC Holdings in favour of other HSBC Group entities
	US$m	**US$m**	US$m	US$m
Guarantee type				
Guarantees of indebtedness including financial guarantees[1] and guarantees of a capital nature	**21,175**	**46,988**	23,558	35,073
Standby letters of credit that are financial guarantees	**8,033**	**–**	10,712	–
Other direct credit substitutes[2]	**6,555**	**–**	4,676	–
Performance bonds[3]	**15,367**	**–**	14,468	–
Bid bonds[3]	**927**	**–**	728	–
Standby letters of credit related to particular transactions[3]	**6,263**	**–**	4,944	–
Other transaction-related guarantees[3]	**12,746**	**–**	13,577	–
Other items	**91**	**–**	722	–
	71,157	**46,988**	73,385	35,073

1 *Financial guarantees are contracts that require the issuer to make specified payments to reimburse the holder for a loss incurred because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.*
2 *Other direct credit substitutes include re-insurance letters of credit and trade-related letters of credit issued without provision for the issuing entity to retain title to the underlying shipment.*
3 *Performance bonds, bid bonds, standby letters of credit and other transaction-related guarantees are undertakings by which the obligation on HSBC to make payment depends on the outcome of a future event.*

The amounts disclosed in the above table are nominal principal amounts and reflect HSBC's maximum exposure under a large number of individual guarantee undertakings. The risks and exposures arising from guarantees are captured and managed in accordance with HSBC's overall credit risk management policies and procedures. Approximately half of the above guarantees have a term of less than one year. Guarantees with terms of more than one year are subject to HSBC's annual credit review process.

Financial Services Compensation Scheme

The Financial Services Compensation Scheme ('FSCS') has provided compensation to consumers following the collapse of a number of deposit takers. The compensation paid out to consumers is currently funded through loans from the Bank of England and HM Treasury. HSBC Bank could be liable to pay a proportion of the outstanding borrowings that the FSCS has borrowed from HM Treasury which at 31 March 2010 stood at approximately £20bn (US$30bn). Currently, the levy paid by the bank represents its share of the interest on these borrowings. The accrual at 31 December 2010 was US$144m in respect of the 2010/11 and 2011/12 levy years (2009: US$182m in respect of the 2009/10 and 2010/11 levy years).

The ultimate FSCS levy to the industry as a result of the collapses cannot currently be estimated reliably as it is dependent on various uncertain factors including the potential recoveries of assets by the FSCS and changes in the interest rate, the level of protected deposits and the population of FSCS members at the time.

Commitments

In addition to the commitments disclosed on page 358, at 31 December 2010, HSBC had US$1,071m (2009: US$1,359m) of capital commitments contracted but not provided for and US$287m (2009: US$227m) of capital commitments authorised but not contracted for.

Associates

HSBC's share of associates' contingent liabilities amounted to US$25,640m at 31 December 2010 (2009: US$19,770m). No matters arose where HSBC was severally liable.

42 Lease commitments

Finance lease commitments

HSBC leases land and buildings (including branches) and equipment from third parties under finance lease arrangements to support its operations.

	At 31 December 2010			At 31 December 2009		
	Total future minimum payments US$m	**Future interest charges US$m**	**Present value of finance lease commitments US$m**	Total future minimum payments US$m	Future interest charges US$m	Present value of finance lease commitments US$m
Lease commitments:						
– no later than one year	**107**	**(20)**	**87**	103	(29)	74
– later than one year and no later than five years	**187**	**(92)**	**95**	249	(116)	133
– later than five years	**390**	**(118)**	**272**	619	(182)	437
	684	**(230)**	**454**	971	(327)	644

At 31 December 2010, future minimum sublease payments of US$436m (2009: US$512m) are expected to be received under non-cancellable subleases at the balance sheet date.

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Operating lease commitments

At 31 December 2010, HSBC was obligated under a number of non-cancellable operating leases for properties, plant and equipment on which the future minimum lease payments extend over a number of years.

	At 31 December 2010		At 31 December 2009	
	Land and buildings US$m	Equipment US$m	Land and buildings US$m	Equipment US$m
Future minimum lease payments under non-cancellable operating leases:				
– no later than one year	920	23	846	11
– later than one year and no later than five years	2,663	37	2,253	11
– later than five years	2,614	–	2,534	–
	6,197	60	5,633	22

At 31 December 2010, future minimum sublease payments of US$21m (2009: US$21m) are expected to be received under non-cancellable subleases at the balance sheet date.

In 2010, US$888m (2009: US$1,100m; 2008: US$861m) was charged to 'General and administrative expenses' in respect of lease and sublease agreements, of which US$869m (2009: US$833m; 2008: US$635m) related to minimum lease payments, US$18m (2009: US$16m; 2008: US$22m) to contingent rents, and US$1m (2009: US$251m; 2008: US$204m) to sublease payments.

The contingent rent represents escalation payments made to landlords for operating, tax and other escalation expenses.

Finance lease receivables

HSBC leases a variety of assets to third parties under finance leases, including transport assets (such as aircraft), property and general plant and machinery. At the end of lease terms, assets may be sold to third parties or leased for further terms. Lessees may participate in any sales proceeds achieved. Lease rentals arising during the lease terms will either be fixed in quantum or be varied to reflect changes in, for example, tax or interest rates. Rentals are calculated to recover the cost of assets less their residual value, and earn finance income.

	At 31 December 2010			At 31 December 2009		
	Total future minimum payments US$m	Unearned finance income US$m	Present value US$m	Total future minimum payments US$m	Unearned finance income US$m	Present value US$m
Lease receivables:						
– no later than one year	3,002	(344)	2,658	2,874	(328)	2,546
– later than one year and no later than five years	8,940	(813)	8,127	9,525	(1,061)	8,464
– later than five years	6,629	(1,462)	5,167	6,902	(1,737)	5,165
	18,571	(2,619)	15,952	19,301	(3,126)	16,175

At 31 December 2010, unguaranteed residual values of US$243m (2009: US$230m) had been accrued, and the accumulated allowance for uncollectible minimum lease payments receivable amounted to US$11m (2009: US$21m). During the year, no contingent rents were received (2009: nil) and recognised in the income statement.

Operating lease receivables

HSBC leases a variety of different assets to third parties under operating lease arrangements, including transport assets, property and general plant and machinery.

	At 31 December 2010		At 31 December 2009	
	Land and buildings US$m	**Equipment US$m**	Land and buildings US$m	Equipment US$m
Future minimum lease payments under non-cancellable operating leases:				
– no later than one year	**18**	**17**	37	857
– later than one year and no later than five years	**21**	**22**	21	917
– later than five years	**14**	**2**	23	447
	53	**41**	81	2,221

43 Special purpose entities

HSBC enters into certain transactions with customers in the ordinary course of business which involve the establishment of special purpose entities ('SPE's) to facilitate or secure customer transactions. HSBC structures that utilise SPEs are authorised centrally when they are established to ensure appropriate purpose and governance. The activities of SPEs administered by HSBC are closely monitored by senior management.

SPEs are assessed for consolidation in accordance with the accounting policy set out in Note 1f.

Total consolidated assets held by SPEs by balance sheet classification

	Conduits US$bn	**Securit-isations US$bn**	**Money market funds US$bn**	**Non-money market investment funds US$bn**	**Total US$bn**
At 31 December 2010					
Cash	**1.0**	**0.7**	**–**	**0.3**	**2.0**
Trading assets	**0.1**	**0.6**	**0.4**	**0.5**	**1.6**
Financial assets designated at fair value	**0.1**	**–**	**–**	**6.4**	**6.5**
Derivatives	**–**	**0.3**	**–**	**–**	**0.3**
Loans and advances to banks	**–**	**1.4**	**–**	**–**	**1.4**
Loans and advances to customers	**8.4**	**22.2**	**–**	**–**	**30.6**
Financial investments	**30.5**	**0.1**	**–**	**–**	**30.6**
Other assets	**1.6**	**0.4**	**–**	**0.4**	**2.4**
	41.7	**25.7**	**0.4**	**7.6**	**75.4**
At 31 December 2009					
Cash	–	–	–	0.2	0.2
Trading assets	–	0.9	42.8	0.2	43.9
Financial assets designated at fair value	0.1	–	–	5.3	5.4
Derivatives	–	1.2	–	–	1.2
Loans and advances to banks	0.3	–	–	–	0.3
Loans and advances to customers	10.3	35.4	–	–	45.7
Financial investments	31.4	–	–	–	31.4
Other assets	1.6	1.4	0.3	–	3.3
	43.7	38.9	43.1	5.7	131.4

HSBC's maximum exposure to SPEs

The following table shows the total assets of the various types of SPEs and the amount of funding provided by HSBC to these SPEs. The table also shows HSBC's maximum exposure to the SPEs and, within that exposure, the liquidity and credit enhancements provided by HSBC. The maximum exposures to SPEs represent HSBC's maximum possible risk exposure that could occur as a result of the Group's arrangements and commitments to SPEs. The maximum amounts are contingent in nature, and may arise as a result of drawdowns under liquidity facilities, where these have been provided, and any other funding commitments, or as a result of any loss protection provided by HSBC to the SPEs. The conditions under which such exposure might arise differ depending on the nature of each SPE and HSBC's involvement with it.

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43 – Special purpose entities

Total assets of consolidated and unconsolidated SPEs and HSBC's funding and maximum exposure

	Consolidated SPEs				Unconsolidated SPEs		
	Total assets US$bn	Funding provided by HSBC US$bn	Liquidity and credit enchance-ments US$bn	HSBC's maximum exposure US$bn	Total assets US$bn	Funding provided by HSBC US$bn	HSBC's maximum exposure US$bn
At 31 December 2010							
Conduits	**41.7**	**28.6**	**38.3**	**50.5**	**–**	**–**	**–**
Securities investment conduits	**32.2**	**28.6**	**25.6**	**37.8**	**–**	**–**	**–**
Multi-seller conduits	**9.5**	**0.0**	**12.7**	**12.7**	**–**	**–**	**–**
Securitisations	**25.7**	**1.9**	**0.1**	**4.7**	**9.9**	**–**	**–**
Money market funds	**0.4**	**0.4**	**–**	**0.4**	**95.8**	**0.7**	**0.7**
Constant net asset value funds	**–**	**–**	**–**	**–**	**74.9**	**0.5**	**0.5**
Other	**0.4**	**0.4**	**–**	**0.4**	**20.9**	**0.2**	**0.2**
Non-money market investment funds	**7.6**	**6.9**	**–**	**6.9**	**274.7**	**1.7**	**1.7**
	75.4	**37.8**	**38.4**	**62.5**	**380.4**	**2.4**	**2.4**
At 31 December 2009							
Conduits	43.7	32.8	43.5	56.9	–	–	–
Securities investment conduits	32.8	32.4	29.1	42.5	–	–	–
Multi-seller conduits	10.9	0.4	14.4	14.4	–	–	–
Securitisations	38.9	2.9	0.1	7.9	11.1	0.1	0.1
Money market funds	43.1	1.5	–	1.5	55.9	0.3	0.3
Constant net asset value funds	42.4	0.9	–	0.9	31.2	0.1	0.1
Other	0.7	0.6	–	0.6	24.7	0.2	0.2
Non-money market investment funds	5.7	5.4	–	5.4	249.7	1.4	1.4
Other	–	–	–	–	20.6	8.8	3.2
	131.4	42.6	43.6	71.7	337.3	10.6	5.0

Conduits

HSBC sponsors and manages two types of conduits: securities investment conduits ('SIC's) and multi-seller conduits.

Securities investment conduits

Solitaire, HSBC's principal SIC, purchases highly rated asset-backed securities ('ABS's) to facilitate tailored investment opportunities. At 31 December 2010, Solitaire held US$11.7bn of ABSs (2009: US$11.7bn). These are included within the disclosures of ABS 'held through consolidated SPEs' on page 133. HSBC's other SICs, Mazarin, Barion and Malachite, evolved from the restructuring of HSBC's sponsored structured investment vehicles ('SIV's) in 2008.

Solitaire

Commercial Paper ('CP') issued by Solitaire benefits from a 100% liquidity facility provided by HSBC. At 31 December 2010, US$7.6bn of Solitaire's assets were funded by the draw-down of the liquidity facility (2009: US$7.6bn). HSBC is exposed to credit losses on the drawn amounts.

HSBC's maximum exposure represents the risk that HSBC may be required to fund the vehicle in the event the CP is redeemed without reinvestment from third parties. At 31 December 2010 this amounted to US$16.8bn (31 December 2009: US$18.4bn).

Mazarin

HSBC is exposed to the par value of Mazarin's assets through the provision of a liquidity facility equal to the lesser of the amortised cost of issued senior debt and the amortised cost of non-defaulted assets. At 31 December 2010 this amounted to US$11.6bn (2009: US$13.6bn). First loss protection is provided through the capital notes issued by Mazarin, which are substantially all held by third parties.

At 31 December 2010, HSBC held 1.3% of Mazarin's capital notes (2009: 1.3%) which have a par value of US$17m (2009: US$17m) and a carrying amount of US$0.6m (2009: US$0.6m).

Barion and Malachite

HSBC's primary exposure to these SICs is represented by the amortised cost of the debt required to support the non-cash assets of the vehicles. At 31 December 2010 this amounted to US$9.4bn (2009: US$10.5bn). First loss protection is provided through the capital notes issued by these vehicles, which are substantially all held by third parties.

At 31 December 2010, HSBC held 3.7% of the capital notes issued by these vehicles (2009: 3.8%) which have a par value of US$35m (2009: US$37m) and a carrying amount of US$2m (2009: US$2m).

Multi-seller conduits

These vehicles were established for the purpose of providing access to flexible market-based sources of finance for HSBC's clients.

HSBC's maximum exposure is equal to the transaction-specific liquidity facilities offered to the multi-seller conduits. First loss protection is provided by the originator of the assets, and not by HSBC, through transaction-specific credit enhancements. A layer of secondary loss protection is provided by HSBC in the form of programme-wide enhancement facilities.

The following table sets out the weighted average life of the asset portfolios for the above mentioned conduits.

Weighted average life of portfolios

Weighted average life (years)	Solitaire	Other SICs	Total SICs	Total multi-seller conduits
At 31 December 2010	**5.1**	**4.0**	**4.4**	**1.8**
At 31 December 2009	6.3	4.1	4.9	2.4

Securitisations

HSBC uses SPEs to securitise customer loans and advances that it has originated in order to diversify its sources of funding for asset origination and for capital efficiency purposes. The loans and advances are transferred by HSBC to the SPEs for cash, and the SPEs issue debt securities to investors to fund the cash purchases.

HSBC's maximum exposure is the aggregate of any holdings of notes issued by these vehicles and the reserve account positions intended to provide credit support under certain pre-defined circumstances to senior note holders.

In addition, HSBC uses SPEs to mitigate the capital absorbed by some of the customer loans and advances it has originated. Credit derivatives are used to transfer the credit risk associated with these customer loans and advances to an SPE, using securitisations commonly known as synthetic securitisations by which the SPE writes credit default swap protection to HSBC. The SPE is funded by the issuance of notes with the cash held as collateral against the credit default protection. From a UK regulatory perspective, the credit protection issued by the SPE in respect of the customer loans allows the risk weight of the loans to be replaced by the risk weight of the collateral in the SPE and as a result mitigates the capital absorbed by the customer loans. Any notes issued by the SPE and held by HSBC attract the appropriate risk weight under the relevant regulatory regime. These SPEs are consolidated when HSBC is exposed to the majority of risks and rewards of ownership.

Money market funds

HSBC has established and manages a number of money market funds which provide customers with tailored investment opportunities within narrow and well-defined objectives.

The majority of these money market funds are Constant Net Asset Value funds ('CNAV'), which invest in shorter-dated and highly-rated money market securities with the objective of providing investors with a highly liquid and secure investment. In September 2008 during the financial crisis, HSBC consolidated certain of its CNAV funds as a result of a number of actions taken to maintain their AAA rating and mitigate the risks of forced sales of liquid assets to meet potential redemptions. Since consolidation of the CNAV funds, HSBC has not provided any additional support to the funds and letters of indemnity provided in 2008 have all expired. At all times the funds continued to be governed by their prospectuses.

In December 2010, management determined that it would not provide similar support in the future in the light of changes in the application of banking regulations. As a result, any presumption of ongoing support caused by past actions is no longer valid and it is not appropriate to continue to consolidate the CNAV funds.

The effect of deconsolidating the CNAV funds on HSBC's balance sheet was to derecognise US$44.4bn of assets and US$43.9bn of liabilities. The deconsolidation of the CNAV funds did not have a material impact on HSBC's consolidated income statement for the year ended 31 December 2010.

HSBC's maximum exposure to the CNAV funds is represented by HSBC's investment in the units of the funds which at 31 December 2010 amounted to US$0.5bn (2009: US$1.0bn). Investments in units of the funds are included within 'Trading assets'. Prior to deconsolidation, the interest income from the CNAV funds and the expense payable to third-party holders of units in the funds were presented within 'Net interest income on trading activities'.

HSBC's maximum exposure to money market funds is represented by HSBC's investment in the units of each fund, which at 31 December 2010 amounted to US$1.1bn (2009: US$1.8bn).

Non-money market investment funds

HSBC has established a large number of non-money market investment funds to enable customers to invest in a range of assets, typically equities and debt securities.

HSBC's maximum exposure to non-money market investment funds is represented by its investment in the units of each fund which at 31 December 2010 amounted to US$8.6bn (2009: US$6.8bn).

Other

HSBC also establishes SPEs in the normal course of business for a number of purposes, for example, structured credit transactions for customers, to provide finance to public and private sector infrastructure projects, and for asset and structured finance transactions.

In certain transactions HSBC is exposed to risk often referred to as gap risk. Gap risk typically arises in transactions where the aggregate potential claims against the SPE by HSBC pursuant to one or more derivatives could be greater than the value of the collateral held by the SPE and securing such derivatives. HSBC often mitigates such gap risk by incorporating in the SPE transaction features which allow for deleveraging, a managed liquidation of the portfolio, or other mechanisms including trade restructuring or unwinding the trade. Following the inclusion of such risk reduction mechanisms, HSBC has, in certain circumstances, retained all or a portion of the underlying exposure in the transaction. In these circumstances, HSBC assesses whether the exposure retained causes a requirement under IFRSs to consolidate the SPE. When this retained exposure represents ABSs, it has been included in 'Nature of HSBC's exposures' on page 129.

Third-party sponsored SPEs

Through standby liquidity facility commitments, HSBC has exposure to third-party sponsored SIVs, conduits and securitisations under normal banking arrangements on standard market terms. These exposures are not considered significant to HSBC's operations.

Additional off-balance sheet arrangements and commitments

Additional off-balance sheet commitments such as financial guarantees, letters of credit and commitments to lend are disclosed in Note 41.

Leveraged finance transactions

Loan commitments in respect of leveraged finance transactions are accounted for as derivatives where it is HSBC's intention to sell the loan after origination. Further information is provided on pages 138 and 139.

44 Legal proceedings, investigations and regulatory matters

HSBC is party to legal proceedings, investigations and regulatory matters in a number of jurisdictions including the UK, Hong Kong and the US arising out of its normal business operations. Apart from the matters described below, HSBC considers that none of these matters is material, either individually or in the aggregate. HSBC recognises a provision for a liability in relation to these matters when it is probable that an outflow of economic benefits will be required to settle an obligation which has arisen as a result of past events, and for which a reliable estimate can be made of the amount of the obligation. While the outcome of these matters is inherently uncertain, management believes that, based on the information available to it, appropriate provisions have been made in respect of legal proceedings, investigations and regulatory matters as at 31 December 2010 (see note 33, Provisions).

Securities litigation

As a result of an August 2002 restatement of previously reported consolidated financial statements and other corporate events, including the 2002 settlement with 46 State Attorneys General relating to real estate lending practices, Household International (now HSBC Finance) and certain former officers were named as defendants in a class action law suit, *Jaffe v Household International Inc, et al* No 2. C 5893 (N.D.Ill, filed 19 August 2002). The complaint asserted claims under the US Securities Exchange Act of 1934, on behalf of all persons who acquired and disposed of Household International common stock between 30 July 1999 and 11 October 2002. The claims alleged that the defendants knowingly or recklessly made false and misleading statements of material fact relating to Household's Consumer Lending operations, including collections, sales and lending practices, some of which ultimately led to the 2002 State settlement agreement, and facts relating to accounting practices evidenced by the restatement. Following a jury trial concluded in April 2009, which was decided partly in favour of the plaintiffs, the Court issued a ruling on 22 November 2010, within the second phase of the case to determine actual damages, that claim forms should be mailed to class members, and also set out a method for calculating damages for class members who filed claims. At subsequent hearings the Court has allowed HSBC Finance to take limited discovery on the issue of whether investors relied on the 'misleading statements' at the time they made their investments and also reserved on the issue of whether HSBC Finance would ultimately be entitled to a jury trial on the issue of reliance.

Despite the jury verdict and the 22 November 2010 ruling, HSBC continues to believe that it has meritorious defences, and intends to seek an appeal of the Court's rulings. Lead Plaintiffs, in Court filings, have estimated that damages could range 'somewhere between US$2.4bn to US$3.2bn to class members', before pre-judgement interest. The timing and outcome of the resolution of this matter is uncertain. Given the complexity and uncertainties associated with the actual determination of damages, including but not limited to the number of class members that may file valid claims, the number of claims that can be substantiated by class members providing adequate documentation, the reduction of trading losses by any trading gains made over the relevant period, the determination of reliance by class members on the financial statements, and whether any given class member was the beneficial owner of the shares, HSBC is unable at this time to estimate reliably the amount of any damages, or range of possible damages, that could arise, but they could be significant.

Bernard L. Madoff Investment Securities LLC

In December 2008, Bernard L. Madoff ('Madoff') was arrested for running a Ponzi scheme and a trustee was appointed for the liquidation of his firm, Bernard L. Madoff Investment Securities LLC ('Madoff Securities'), an SEC-registered broker-dealer and investment adviser. Since his appointment, the trustee has been recovering assets and processing claims of Madoff Securities customers. Madoff subsequently pleaded guilty to various charges and is serving a 150-year prison sentence. He has acknowledged, in essence, that while purporting to invest his customers' money in securities and, upon request, return their profits and principal, he in fact never invested in securities and used other customers' money to fulfil requests for the return of profits and principal. The relevant US authorities are continuing their investigations into his fraud, and have brought charges against others.

Various non-US HSBC companies provided custodial, administration and similar services to a number of funds incorporated outside the US whose assets were invested with Madoff Securities.

Based on information provided by Madoff Securities, as at 30 November 2008, the purported aggregate value of these funds was US$8.4bn, an amount that includes fictitious profits reported by Madoff. Based on information available to HSBC to date, we estimate that the funds' actual transfers to Madoff Securities minus their actual withdrawals from Madoff Securities during the time that HSBC serviced the funds totalled approximately US$4.3bn.

Plaintiffs (including funds, fund investors, and the Madoff Securities trustee) have commenced Madoff-related proceedings against numerous defendants in a multitude of jurisdictions. Various HSBC companies have been named as defendants in suits in the US, Ireland, Luxembourg, and other jurisdictions. The suits (which include US class actions) allege that the HSBC defendants knew or should have known of Madoff's fraud and breached various duties to the funds and fund investors. In December 2010, the Madoff Securities trustee commenced suits against various HSBC companies in the US bankruptcy court and in the English High Court. The US action (which also names certain funds, investment managers, and other entities and individuals) seeks US$9bn in damages and additional recoveries from HSBC and the various co-defendants. It seeks damages against HSBC for allegedly aiding and abetting Madoff's fraud and breach of fiduciary duty. It also seeks, pursuant to US bankruptcy law, recovery of unspecified amounts received by HSBC from funds invested with Madoff, including amounts that HSBC received when it redeemed units HSBC held in the various funds. HSBC acquired those fund units in connection with financing transactions HSBC had entered into with various clients. The trustee's US bankruptcy law claims also seek recovery of fees earned by HSBC for providing custodial, administration and similar services to the funds. The trustee's English action seeks recovery of unspecified transfers of money from Madoff Securities to or through HSBC, on the ground that the HSBC defendants actually or constructively knew of Madoff's fraud.

Between October 2009 and July 2010, Fairfield Sentry Limited and Fairfield Sigma Limited ('Fairfield'), funds whose assets were directly or indirectly invested with Madoff Securities, commenced multiple suits in the British Virgin Islands and the US against numerous fund shareholders, including various HSBC companies that acted as nominees for clients of HSBC's private banking business and other clients who invested in the Fairfield funds. The Fairfield actions seek restitution of amounts paid to the defendants in connection with share redemptions, on the ground that such payments were made by mistake, based on inflated values resulting from Madoff's fraud.

There are many factors which may affect the range of possible outcomes, and the resulting financial impact, of the various Madoff-related proceedings, including but not limited to the circumstances of the fraud, the multiple jurisdictions in which the proceedings have been brought and the number of different plaintiffs and defendants in such proceedings. The cases where HSBC companies are named as a defendant are at an early stage. For these reasons, among others, it is not practicable at this time for HSBC to estimate reliably the aggregate liabilities, or ranges of liabilities, that might arise as a result of all such claims but they could be significant. In any event, HSBC considers that it has good defences to these claims and will continue to defend them vigorously.

Payment Protection Insurance

Following an extensive period of consultation, on 10 August 2010 the Financial Services Authority ('FSA') published Policy Statement 10/12 ('PS 10/12') on the assessment and redress of Payment Protection Insurance ('PPI') complaints. This included (i) new handbook guidance setting out how complaints are to be handled, and 'redressed fairly' where appropriate; (ii) an explanation of when and why firms should analyse their past complaints to identify if there are serious flaws in sales practices that may have affected complainants and non-complainants; and (iii) an Open Letter setting out common sales failings to help firms identify bad practices.

After extensive consideration, the British Bankers Association ('BBA'), as the representative body of UK banks, sent a formal pre-action protocol letter to the FSA and the Financial Ombudsman Service ('FOS') setting out its concerns and what it considered to be the flaws identified in PS 10/12 and Guidance issued by FOS on the handling of PPI complaints. The letter indicated that, absent a satisfactory reply, it was the BBA's intention to apply to the High Court for a Judicial Review of both PS 10/12 and the FOS Guidance. The FSA and FOS responded on 28 September 2010 denying that they had acted unlawfully in introducing the Policy Statement or relying on the Guidance.

On 8 October 2010, an application for Judicial Review was issued by the BBA seeking an order to quash PS 10/12 and the FOS Guidance. The FSA subsequently issued a statement on 24 November 2010 seeking to clarify aspects of PS 10/12 and the Open Letter. The FSA and FOS filed defences to the Judicial Review application on 10 December 2010. The Judicial Review application was heard by the Court on 25 – 28 January 2011, and judgement is currently awaited.

HSBC believes that the BBA has a strongly arguable case against both the FSA and the FOS. If the Court ultimately concludes, however, after any appeals of the judgement that may follow from any of the parties, that PS 10/12 and the FOS Guidance stand, in whole or in part, then these would need to be taken into consideration when determining complaints alleging the mis-sale of PPI.

If, contrary to HSBC's current assessment, a decision is reached in the case that results in a potential liability for HSBC, a large number of different outcomes is possible, each of which would have a different financial impact.

There are many factors affecting the range of possible outcomes, and the resulting financial impact, including the extent to which one or both of PS 10/12 and the FOS Guidance are upheld, and the underlying rationale for each decision; the ways in which PS 10/12 and or the FOS Guidance are found to impose additional requirements over and above the common law and the FSA Conduct of Business rules in force at the time relating to the sale of general insurance products, and in the handling of firms' PPI complaints; the effect of any decision on the nature and volume of customer complaints; and the extent to which, if at all, HSBC might be required to take action, and the nature of any such action, in relation to non-complainants. The extent of any redress that may be required as a result of a decision to uphold PS 10/12 and the FOS Guidance, in whole or in part, would also depend on the facts and circumstances of each individual customer's case. For these reasons, among others, HSBC does not at this time consider it practicable to provide a reliable estimate or range of estimates of the potential financial impact of an adverse decision.

Pending resolution of the dispute, HSBC continues to review all complaints received which allege that PPI has been mis-sold and, where possible, seeks to resolve them. Where HSBC considers it is not in a position to reach a final decision on a complaint until the conclusion of the application for Judicial Review of PS 10/12 and the FOS Guidance and any subsequent appeals, it informs the complainant that this is the case.

In December 2007, the Group decided to cease selling PPI products in the UK and a phased withdrawal was completed across the HSBC, first direct and M&S Money brands during 2008. HFC Bank Ltd ('HFC') ceased selling single premium PPI in 2008 and sales of regular premium PPI will reduce as HFC exits its remaining retail relationships. During the consultation process in 2009, the FSA reported that it had obtained agreement from firms representing 40% of the market for face to face single premium PPI sales to review all such sales since July 2007. No HSBC subsidiary or associate was included in that group of firms.

Regulatory and law enforcement agencies investigations

HSBC Bank USA entered into a consent cease and desist order with the Office of the Comptroller of the Currency and the indirect parent of that company, HSBC North America, entered into a consent cease and desist order with the Federal Reserve Board in the first week of October 2010. These actions require improvements for an effective compliance risk management programme across the Group's US businesses, including US Bank Secrecy Act ('BSA') and Anti Money Laundering ('AML') compliance. Steps continue to be taken to address the requirements of these Orders and to ensure that compliance and effective policies and procedures are maintained.

Various HSBC Group companies are the subject of ongoing investigations, including Grand Jury subpoenas and other requests for information, by US Government agencies, including the US Attorney's Office, the US Department of Justice and the New York County District Attorney's Office. These investigations pertain to, among other matters, HSBC Bank USA's bank note and foreign correspondent banking businesses and its compliance with BSA and AML controls, as well as various HSBC companies' compliance with Office of Foreign Asset Control ('OFAC') requirements, and adherence by certain customers to US tax reporting requirements.

The consent cease and desist orders do not preclude additional enforcement actions against HSBC Bank USA or HSBC North America by bank regulatory or law enforcement agencies, including actions to recover civil money penalties, fines and other financial penalties relating to activities which were the subject of the cease and desist orders. In addition, it is likely that there could be some form of formal enforcement action in respect of some or all of the ongoing investigations. Actual or threatened enforcement actions against other financial institutions for breaches of BSA, AML and OFAC requirements have resulted in settlements involving fines and penalties, some of which have been significant depending on the individual circumstances of each action. The ongoing investigations are at an early stage. Based on the facts currently known, it is not practicable at this time for HSBC to determine the terms on which the ongoing investigations will be resolved or the timing of such resolution or for HSBC to estimate reliably the amounts, or range of possible amounts, of any fines and/or penalties. As matters progress, it is possible that any fines and/or penalties could be significant.

45 Related party transactions

Related parties of the Group and HSBC Holdings include subsidiaries, associates, joint ventures, post-employment benefit plans for HSBC employees, Key Management Personnel, close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced, or for which significant voting power is held, by Key Management Personnel or their close family members.

Key Management Personnel are defined as those persons having authority and responsibility for planning, directing and controlling the activities of HSBC Holdings, being the Directors and Group Managing Directors of HSBC Holdings.

Compensation of Key Management Personnel

	HSBC		
	2010 US$m	2009 US$m	2008 US$m
Short-term employee benefits	**39**	22	31
Post-employment benefits	**3**	3	5
Other long-term benefits	**1**	–	–
Termination benefits	**–**	–	–
Share-based payments	**49**	27	16
	92	52	52

Transactions, arrangements and agreements involving related parties

Particulars of advances (loans and quasi-loans), credits and guarantees entered into by subsidiaries of HSBC Holdings during 2010 with Directors, disclosed pursuant to section 413 of the Companies Act 2006, are shown below:

	At 31 December	
	2010 US$m	2009 US$m
Advances and credits	**9**	5

Particulars of transactions with related parties, disclosed pursuant to the requirements of IAS 24, are shown below. The disclosure of the year-end balance and the highest amounts outstanding during the year in the table below is considered to be the most meaningful information to represent the amount of the transactions and the amount of outstanding balances during the year.

	2010		2009	
	Balance at 31 December US$m	**Highest amounts outstanding during year US$m**	Balance at 31 December US$m	Highest amounts outstanding during year US$m
Key Management Personnel[1]				
Advances and credits	**901**	**1,681**	736	1,407
Guarantees	**27**	**31**	32	34

1 *Includes Key Management Personnel, close family members of Key Management Personnel and entities which are controlled, jointly controlled or significantly influenced, or for which significant voting power is held, by Key Management Personnel or their close family members.*

Some of the transactions were connected transactions, as defined by the Rules Governing The Listing of Securities on The Stock Exchange of Hong Kong Limited but were exempt from any disclosure requirements under the provisions of those Rules. The above transactions were made in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with persons of a similar standing or, where applicable, with other employees. The transactions did not involve more than the normal risk of repayment or present other unfavourable features.

Shareholdings, options and other securities of Key Management Personnel

	At 31 December	
	2010 (000s)	2009 (000s)
Number of options held over HSBC Holdings ordinary shares under employee share plans	**602**	1,033
Number of HSBC Holdings ordinary shares held beneficially and non-beneficially	**13,395**	19,567
Number of HSBC Holdings preference shares held beneficially and non-beneficially	**–**	8
Number of HSBC Holdings 8.125% Perpetual Subordinated Capital Securities held beneficially and non-beneficially	**–**	25
	13,997	20,633

Transactions with other related parties of HSBC

Associates and joint ventures

The Group provides certain banking and financial services to associates and joint ventures, including loans, overdrafts, interest and non-interest bearing deposits and current accounts. Details of the interests in associates and joint ventures are given in Note 21. Transactions and balances during the year with associates and joint ventures were as follows:

	2010		2009	
	Highest balance during the year[1] US$m	**Balance at 31 December[1] US$m**	Highest balance during the year[1] US$m	Balance at 31 December[1] US$m
Amounts due from joint ventures:				
– subordinated	**5**	**5**	–	–
– unsubordinated	**514**	**412**	423	378
Amounts due from associates:				
– subordinated	**16**	**–**	17	17
– unsubordinated	**2,248**	**1,702**	1,343	1,239
	2,783	**2,119**	1,783	1,634
Amounts due to joint ventures	**151**	**134**	130	129
Amounts due to associates	**700**	**527**	1,494	136
	851	**661**	1,624	265

1 *The disclosure of the year-end balance and the highest balance during the year is considered the most meaningful information to represent transactions during the year.*

The above outstanding balances arose from the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with third-party counterparties.

Post-employment benefit plans

At 31 December 2010, US$4.7bn (2009: US$4.2bn) of HSBC post-employment benefit plan assets were under management by HSBC companies. Fees of US$17m (2009: US$15m) were earned by HSBC companies for these management services provided to its post-employment benefit plans. HSBC's post-employment benefit plans had placed deposits of US$1,840m (2009: US$929m) with its banking subsidiaries, on which interest payable to the schemes amounted to US$4m (2009: US$3m). The above outstanding balances arose from the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with third-party counterparties.

HSBC Bank (UK) Pension Scheme entered into swap transactions with HSBC as part of the management of the inflation and interest rate sensitivity of its liabilities. At 31 December 2010, the gross notional value of the swaps was US$22.9bn (2009: US$23.7bn), the swaps had a positive fair value of US$2.2bn (2009: positive fair value of US$1.0bn) to the scheme and HSBC had delivered collateral of US$3.3bn (2009: US$2.8bn) to the scheme in respect of these swaps, on which HSBC earned interest amounting to nil (2009: US$7m). All swaps were executed at prevailing market rates and within standard market bid/offer spreads.

In order to satisfy diversification requirements, there are special collateral provisions for the swap transactions between HSBC and the scheme. The collateral agreement stipulates that the scheme never posts collateral to HSBC.

Collateral is posted to the scheme by HSBC at an amount that provides the Trustee with a high level of confidence that would be sufficient to replace the swaps in the event of default by HSBC Bank plc. With the exception of the special collateral arrangements detailed above, all other aspects of the swap transactions between HSBC and the scheme are on substantially the same terms as comparable transactions with third-party counterparties.

On 17 June 2010, HSBC Bank plc made a £1,760m (US$2,638m) special contribution to accelerate the reduction of the deficit of the HSBC Bank (UK) Pension Scheme. On the same day the Scheme used the contribution to acquire debt securities with a fair value of £1,760m (US$2,638m) from HSBC in a transaction at an arm's length value determined by the Scheme's independent third-party advisors.

HSBC International Staff Retirements Benefits Scheme entered into swap transactions with HSBC to manage the inflation and interest rate sensitivity of the liabilities and selected assets. At 31 December 2010, the gross notional value of the swaps was US$1.8bn (2009: US$1.8bn) and the swaps had a net positive fair value of US$77m to the scheme (2009: US$27m).

HSBC Holdings

Details of HSBC Holdings' principal subsidiaries are shown in Note 26. Transactions and balances during the year with subsidiaries were as follows:

	2010		2009	
	Highest balance during the year[1]	**Balance at 31 December[1]**	Highest balance during the year[1]	Balance at 31 December[1]
	US$m	**US$m**	US$m	US$m
Assets				
Cash at bank	**459**	**459**	443	224
Derivatives	**3,219**	**2,327**	3,682	2,981
Loans and advances	**23,212**	**21,238**	26,156	23,212
Financial investments	**2,606**	**2,025**	2,629	2,455
Investments in subsidiaries	**92,899**	**92,899**	90,914	86,247
Total related party assets	**122,395**	**118,948**	123,824	115,119
Liabilities				
Amounts owed to HSBC undertakings	**4,580**	**2,932**	5,669	3,711
Derivatives	**1,677**	**827**	1,324	362
Subordinated liabilities:				
– at amortised cost	**3,907**	**2,464**	3,907	3,907
– designated at fair value	**4,507**	**4,259**	4,360	4,360
Total related party liabilities	**14,671**	**10,482**	15,260	12,340
Guarantees	**46,988**	**46,988**	47,341	35,073
Commitments	**3,240**	**2,720**	3,241	3,240

1 *The disclosure of the year-end balance and the highest balance during the year is considered the most meaningful information to represent transactions during the year. The above outstanding balances arose in the ordinary course of business and are on substantially the same terms, including interest rates and security, as for comparable transactions with third-party counterparties, with the exception of US$160m (2009: US$160m) in respect of loans to HSBC subsidiaries from HSBC Holdings and US$506m (2009: US$529m) in respect of loans from HSBC subsidiaries to HSBC Holdings made at an agreed zero per cent interest rate.*

Some employees of HSBC Holdings are members of the HSBC Bank (UK) Pension Scheme, which is sponsored by a separate Group company. HSBC Holdings incurs a charge for these employees equal to the contributions paid into the scheme on their behalf. Disclosure in relation to the scheme is made in Note 7 to the accounts.

46 Events after the balance sheet date

A fourth interim dividend for 2010 of US$0.12 per ordinary share (a distribution of approximately US$2,125m) was declared by the Directors after 31 December 2010.

These accounts were approved by the Board of Directors on 28 February 2011 and authorised for issue.